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OFFICE OF INSPECTOR GENERAL
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Telephone: (404) 562-6470 Fax: (404) 562-6509

Memorandum

DATE: September 25, 2003

TO: Theresa S. Shaw
Chief Operating Officer
Federal Student Aid

FROM: J. Wayne Bynum /s/ J. Wayne Bynum
Regional Inspector General for Audit
Region IV

SUBJECT: **Final Audit Report**
Advanced Career Training Institute's Administration of the Title IV Higher Education Act Programs
Control Number ED-OIG/A04-B0019

You have been designated as the action official responsible for the resolution of the findings and recommendations in the attached final report. We have also provided a copy to the auditee and to your Audit Liaison Officer.

The Office of Inspector General is required to review and approve your proposed Program Determination Letter (PDL) and the Audit Clearance Document (ACD) before the PDL is forwarded to the auditee. Please provide these documents for review, electronically if you wish or by mail, to:

J. Wayne Bynum
Regional Inspector General, Region IV
U.S. Department of Education
Office of Inspector General
61 Forsyth Street, Room 18T71
Atlanta, GA 30303

In accordance with the Inspector General Act of 1978, as amended, the Office of Inspector General is required to report to Congress twice a year on the number of audits unresolved. In addition, any report unresolved after 180 days from the date of issuance will be shown as overdue in our reports to Congress.

In accordance with the Freedom of Information Act (5 U.S.C. §552), reports issued by the Office of Inspector General are available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

If you have any questions, please contact me at 404-562-6477 or Assistant Regional Inspector General Mary Allen at 404-562-6465.

Attachment

Advanced Career Training Institute's Administration of the Title IV Higher Education Act Programs

FINAL AUDIT REPORT

ED-OIG/A04-B0019
September 2003

Our mission is to promote the efficiency, effectiveness, and integrity of the Department's programs and operations.

U.S. Department of Education
Office of Inspector General
Atlanta, Georgia

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. Determinations of corrective action to be taken will be made by the appropriate Department of Education officials.

In accordance with the Freedom of Information Act (5 U.S.C. § 552), reports issued by the Office of Inspector General are available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

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EXECUTIVE SUMMARY

Advanced Career Training Institute (ACT) is a proprietary institution with campuses in Atlanta and Riverdale, GA, and Jacksonville, FL. The purpose of the audit was to determine whether ACT administered the student financial assistance programs in accordance with Title IV of the Higher Education Act (HEA) of 1965, as amended, and applicable regulations. Specifically, we reviewed ACT's compliance with the requirements for (1) institutional eligibility, including the 90/10 Rule, accreditation, and State licensing, (2) cash management, (3) William D. Ford Federal Direct Loan (Direct Loan) reconciliation, (4) refunds and the return of Title IV funds, (5) student eligibility, (6) program length, and (7) commissioned sales. Audit coverage included award years 1998-1999, 1999-2000, and 2000-2001. For purpose of the 90/10 revenue calculations and cash management review, audit coverage included school fiscal years (FY) 1999 through 2001. For program length, audit coverage included school FY 2001. During its school FY's 1999 through 2001, ACT received $23.5 million in Title IV funds.

We identified problems with the 90/10 Rule revenue percentage, cash management, student eligibility, Direct Loan reconciliation, and refunds and the return of funds. Based on the significance of these findings, we concluded that ACT did not meet the administrative capability standards required to participate in the Title IV programs.

To participate in the Title IV programs, at least 10 percent of a proprietary institution's revenues must come from sources that are not derived from funds provided under Title IV (90/10 Rule). ACT determined a 90/10 revenue percentage of 85.1. However, when it calculated the 90/10 revenue percentages, ACT did not properly determine the amount of Title IV revenue used to satisfy tuition, fees, and other institutional charges to students and adjust for credit balances on student accounts and cash paid to students. We determined that ACT's Title IV revenue was 91.6 percent for school FY 1999. Failure to meet the 90/10 Rule in a fiscal year results in ineligibility for the subsequent fiscal year. As a result, ACT was not eligible for the $7.4 million in Title IV funds it received during FY 2000.

Institutions must act with competency and integrity in administering the Title IV programs and in accounting for the funds received. ACT breached its fiduciary responsibility to the Secretary when it used Title IV funds for other than the intended purpose. It was ACT policy to transfer Title IV funds from its Federal Funds account to its operating account one day after the funds were drawn down from the Department. Such transfers are to be done only when the funds are used for their intended purpose (i.e., disbursed to students). ACT did not know who the intended student beneficiaries were for the funds transferred to the operating account. During FY's 1999, 2000, and 2001, Title IV drawdowns transferred to the operating account exceeded the amounts posted to student accounts by almost $995,000.

Title IV funds drawn down from the Department are to be disbursed to students within three business days. Over two-thirds of the student accounts that we reviewed were not posted within three business days after the funds were drawn down. The elapsed days between draw down and disbursement to student accounts ranged from 4 to 648 days.

ACT improperly disbursed $67,744 in Title IV funds to ineligible students by disbursing funds to students more than 90 days after their last date of attendance, making second Direct Loan disbursements to students who had withdrawn from school, and disbursing funds to students who did not pass the ability-to-benefit test.

Direct loan funds are to be reconciled on a monthly basis. ACT did not reconcile Direct Loan awards during FY's 1999 and 2000. ACT officials were attempting to reconcile Direct Loan funds at the time of this audit. ACT returned $900,000 in unaccounted for Direct Loan funds to the Department in October 2001.

Institutions are required to calculate returns of Title IV funds for students who withdraw from school. Of the 51 student files reviewed that required refunds, ACT failed to make refunds for ten students and incorrectly calculated refunds for two students. ACT has a history of refund problems. Its FY 1999 and FY 2000 compliance audits contained findings pertaining to untimely refunds and the failure to make refunds. These findings resulted in the Department requesting a letter of credit for $3.5 million from ACT's parent corporation, International Education Corporation (IEC).

We recommend that the Chief Operating Officer for Federal Student Aid:
- Recover $7.4 million of Title IV funds provided to ACT during FY 2000;
- Recover $67,744[1] in Federal funds improperly disbursed to students and $9,619 for refunds not made or made in the incorrect amount; and
- Impose appropriate action against ACT, up to and including terminating participation in the Title IV student financial assistance programs.

If ACT is allowed to continue to participate in the Title IV programs, we recommend that the Chief Operating Officer for Federal Student Aid require ACT to establish policies, procedures, and management controls to ensure the following:
- The 90/10 Rule revenue percentage is accurately calculated and reported,
- Title IV funds are maintained in the interest-bearing Federal Funds account until the funds are disbursed to students,
- Title IV funds are disbursed to students within three business days,
- Ineligible students do not receive Title IV disbursements,
- Direct Loans are reconciled on a monthly basis, and
- Refunds are calculated accurately and timely returned to the Department.

In its written response to the draft report, a copy of which is included as Attachment B to this report, ACT disagreed that it failed to meet the requirements of the 90/10 Rule for school FY 1999. ACT stated that the report was fundamentally flawed in failing to apply the cash basis of accounting and in the treatment of third-party loans received by certain students. ACT

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[1] $3,852 of this amount was disbursed during school FY 2000. If it is determined that ACT must return the $7.4 million in Title IV funds received during school FY 2000, the $3,852 should be deducted from the $67,744.

accepted OIG's figure for Title IV revenue, but disagreed with some of OIG's figures for non-Title IV revenue. ACT provided supplemental information regarding non-Title IV revenue. Using its revised 90/10 non-Title IV revenue figures, ACT concluded that it met the 90/10 Rule.

ACT agreed that it did not consistently disburse Title IV funds to students in accordance with Departmental requirements. ACT acknowledged that during the period covered by the audit, Title IV funds were not consistently credited to student accounts within three business days. ACT also agreed that it did not reconcile its Direct Loan accounts on a monthly basis during 1988-1999 and 1999-2000 and that subsequent to that time it initiated a reconciliation of its Direct Loan funds.

ACT provided additional information for the students identified as receiving improper Title IV disbursements, and stated that it had implemented various new procedures and provided additional training to its staff to ensure that Title IV funds are not disbursed to ineligible students. ACT also provided additional information for the withdrawn students for which ACT failed to make Title IV refunds or incorrectly calculated refunds.

ACT acknowledged that it had administrative and cash management problems in the past. ACT stated that it tried to demonstrate that is has devoted extensive attention and resources to correcting these problems. Based on the corrective actions taken to address the issues identified in the report, and its current capabilities and processes, ACT does not believe that it should be limited, suspended, or terminated from future participation in the Title IV programs.

We disagree with ACT's position that the cash basis of accounting should be used without regard to when and for what Title IV funds are used. Title IV funds are not used for the purpose intended until the funds are disbursed to students. Also, only Title IV and non-Title IV funds used to satisfy tuition, fees, and other institutional charges within the fiscal year can be included in the annual 90/10 revenue computation. We revised some of the non-Title IV revenue figures based on the additional information provided by ACT. However, based on the revised figures, we found that ACT still failed to meet the 90/10 Rule for school FY 1999. We also made adjustments to Findings 3 and 5 based on ACT's written response to the draft audit report. We summarized ACT's response after each finding and included them in their entirety as Attachment B to this report. ACT also provided supporting documentation with the written response to the draft report, which is available upon request.

AUDIT RESULTS

Our audit objective was to determine whether ACT administered the student financial assistance programs in accordance with Title IV of the Higher Education Act of 1965, as amended, and applicable regulations. Specifically, we reviewed ACT's compliance with the requirements for (1) institutional eligibility, including the 90/10 Rule, accreditation, and State licensing, (2) cash management, (3) Direct Loan reconciliation, (4) refunds and the return of Title IV funds, (5) student eligibility, (6) program length, and (7) commissioned sales. Audit coverage included award years 1998-1999, 1999-2000, and 2000-2001. For purposes of the 90/10 revenue calculation and cash management review, audit coverage included school FY's 1999 through 2001. For program length, audit coverage included school FY 2001.

We did not identify compliance problems with accreditation, licensing, program length, or commissioned sales. However, we identified problems with the 90/10 Rule revenue percentage, cash management, student eligibility, Direct Loan reconciliation, and refunds and the return of funds. Based on the significance of these findings, we concluded that ACT did not meet the administrative capability standards required to participate in the Title IV programs.

Finding No. 1 – ACT Failed to Meet the 90/10 Rule in FY 1999

International Education Corporation (IEC), ACT's parent corporation, did not properly determine the amount of Title IV revenue used to satisfy tuition, fees, and other institutional charges to students when calculating the 90/10 revenue percentages for ACT. IEC also did not properly adjust for credit balances on student accounts or cash payments to students. ACT reported 90/10 calculations of less than 90 percent for school FY's 1999, 2000, and 2001. Although ACT determined a 90/10 revenue percentage of 85.1 for school FY 1999, our calculation for this school fiscal year was 91.6 percent. As a result of failing to meet the 90/10 eligibility requirement for school FY 1999, ACT was ineligible for the $7.4 million in Title IV funds it received for school FY 2000.

Section 102(b) of the Higher Education Act (HEA), as amended, specifies that a proprietary institution of higher education is -

> A school that . . . has at least 10 percent of the school's revenues from sources that are not derived from funds provided under [T]itle IV, as determined in accordance with regulations prescribed by the Secretary.

This institutional eligibility requirement is commonly referred to as the 90/10 Rule. Institutions are required to calculate the 90/10 revenue percent annually. If the result of the calculation is greater than 90 percent, the institution becomes ineligible to participate in the Title IV programs the following year. The regulations at 34 C.F.R. § 600.5(d)(1)[2] provide the following formula to be used in calculating the revenue percentage:

$$\frac{\text{Title IV, HEA program funds the institution used to satisfy tuition, fees, and other institutional charges to students.}}{\text{The sum of revenues generated by the institution from: Tuition, fees, and other institutional charges for students enrolled in eligible programs as defined in 34 CFR [§] 668.8; and activities conducted by the institution, to the extent not included in tuition, fees, and other institutional charges, that are necessary for the education or training of its students who are enrolled in those eligible programs.}}$$

90/10 Revenue Not Properly Calculated
IEC used its CLASS accounting system to calculate the 90/10 revenue percentages. The CLASS system contained the student ledgers, which showed the disbursement of Title IV and non-Title IV funds to student accounts. The CLASS system contained two date fields to indicate the date that students received Title IV and non-Title IV funds. The "transaction date" field contained the date that the disbursement should have occurred per ACT/IEC officials. ACT/IEC staff entered the transaction dates into the CLASS system. The "posting date" field contained the date that the disbursement was actually posted to student accounts. The posting date was automatically generated by the computer system.

IEC used the transaction date data to determine revenue for the 90/10 calculation. As a result of using the transaction date data, the 90/10 calculation did not reflect funds that were actually disbursed to students in the fiscal year. By using the transaction date data, Title IV revenue was understated and non-Title IV revenue was overstated. Attachment A illustrates the extent of the under and overstatements of revenue. To determine revenue for the 90/10 calculation, we used the CLASS system posting date data because it represented the date that funds were actually disbursed to students.

Incorrect Amount for Sallie Mae Recourse Loans Included in the 90/10 Calculation
As a result of using transaction date data, ACT included $745,222 in Student Loan Marketing Association (Sallie Mae) recourse loans as non-Title IV revenue in the 90/10 calculation. We determined that $538,661.90 in Sallie Mae recourse loans was actually posted and disbursed to student accounts during school FY 1999.

According to the terms of the contract with Sallie Mae, IEC was required to deposit 30 percent of the original principal balance of every loan originated into an escrow account. The escrow was funded either by ACT depositing 30 percent or Sallie Mae retaining 30 percent from funds delivered. The contract required ACT to replenish the escrow account if default payments reduced the balance below 20 percent of the principal balance of all outstanding loans. In it's original calculation, ACT excluded $40,124 for the escrow requirement. For our initial 90/10 calculation, we included the Sallie Mae recourse loans posted to student accounts during the fiscal year and adjusted for the full amount (30 percent) required to be escrowed. However, in

[2] Unless otherwise noted, all 34 C.F.R. citations are to the July 1, 1998, volume.

its response to the draft report, ACT provided documentation that $41,259 was deposited in the escrow account during its fiscal year 1999. In finalizing this report, we used the $41,259 figure for the Sallie Mae escrow adjustment in calculating 90/10 revenue (see Attachment A).

Credit Balances and Cash Paid to Students Not Taken into Account for the 90/10 Calculation

IEC included both Title IV and non-Title IV credit balances (funds in excess of what the institution used to satisfy tuition, fees, and other institutional charges) in the 90/10 calculations. ACT also failed to subtract Title IV and non-Title IV cash paid to students.

We used ACT's CLASS system to identify students who had credit balances on their accounts as of the last day of the fiscal year, determined the cause for the credit balances, and adjusted the 90/10 calculation by subtracting the credit balance amounts from the respective category (Title IV or non-Title IV). Funds charged to student accounts in excess of tuition and fees (causing a credit balance) were not used in our 90/10 calculations.

We also used the CLASS system to identify students who received cash payments as a result of credit balances, determined the cause for the cash payments, and adjusted the 90/10 calculation by subtracting the cash payments from the respective category (Title IV or non-Title IV).

90/10 Eligibility Requirement Not Met

The 90/10 revenue originally reported in ACT's audited financial statements was 86.2 percent for FY 1999. Based on its review of the draft audit report, ACT amended some of its revenue figures and computed 90/10 revenue of 85.1 percent. Our calculation of the 90/10 revenue percentage using posting date data and adjusting for credit balances and cash paid to students (and additional non-Title IV revenue documentation provided by ACT as a result of the draft audit report) revealed that ACT's 90/10 percentage was 91.6 for school FY 1999. Since the Title IV revenue percentage for FY 1999 was greater than 90 percent, ACT was not eligible to participate in the Title IV programs for its FY 2000. ACT received $7,399,072 in Title IV funds ($5,201,173 in Direct Loan funds, $2,075,046 in Pell grants, $75,128 in Federal Supplemental Education Opportunity Grant (FSEOG) funds, and $47,725 in Federal Work Study) during its FY 2000. See Attachment A for the 90/10 calculation for FY 1999.

We also performed an alternative 90/10 calculation using Title IV receipts per the Department's Grants Administration Payments System (GAPS) because ACT had not posted student accounts in a timely manner and in some cases not at all. GAPS represents all Title IV fund drawdowns from the Department. If an institution complies with Title IV regulations, all funds drawn down are disbursed to students within three business days. Using the GAPS Title IV draw down figures and making adjustments for funds returned, refunds, and credit balances per the CLASS system posting date data, we calculated a 90/10 revenue percentage of 91.7. (See Attachment A for this calculation.)

During the audit exit conference, ACT/IEC officials said they did not disagree with the facts presented regarding the CLASS accounting system transaction dates being used to calculate the 90/10 revenue percentages. Also, the officials did not disagree that credit balances and cash paid to students should be taken into account for the 90/10 revenue calculations.

RECOMMENDATIONS

We recommend that the Chief Operating Officer for Federal Student Aid require ACT to:

1.1 Return the $7,399,072 of Title IV funds received during the period November 1, 1999, through October 31, 2000.

1.2 Ensure that the 90/10 Rule revenue requirement is accurately calculated by:
- Using the correct date that funds are disbursed to students for the Title IV and non-Title IV revenue portions of the calculation,
- Including the correct amount of Sallie Mae recourse loans in the non-Title IV portion of the calculation, and
- Adjusting for credit balances and cash paid to students.

ACT RESPONSE AND OIG COMMENTS

In its June 21, 2003, written response to the draft audit report, ACT stated that OIG's determination that ACT failed to meet the requirements of the 90/10 Rule for school FY 1999 was based on an incomplete and faulty analysis of the data underlying the school's 90/10 calculation for that year. ACT stated that the report was fundamentally flawed in failing to apply the cash basis of accounting and in the treatment of third-party loans received by certain students. It is ACT's position that it did not fail the 90/10 Rule for school FY 1999. ACT provided a detailed response to the following areas: cash basis of accounting, Sallie Mae loan revenue, Sallie Mae escrow account, Sallie Mae credit balance adjustments, and sale of student retail installment contracts (RIC). ACT's full written response is included as Attachment B.

Cash Basis of Accounting

ACT Response. ACT cited Departmental regulations regarding the requirement for institutions to use the cash basis of accounting whereby revenue is recognized by an entity when that entity receives cash; i.e., the date that the revenue is actually received. ACT cited regulations that require institutions to use the cash basis of accounting in reporting Title IV and non-Title IV revenue for the 90/10 revenue calculation. ACT focused on the point that, in calculating revenue, institutions are required to include Title IV and non-Title IV funds received during the fiscal year. ACT stated that the regulations require no more than that the funds be received by the institution, which is satisfied when the funds are deposited into the institution's bank account.

ACT stated that the issue of how to calculate the Sallie Mae loan revenue in the ratio must be analyzed under the precise terms of the 90/10 Rule, and specifically the requirement to focus on the funds "received" by the institution in the applicable year. By its terms, the regulation requires that the funds be received by the institution, which is satisfied when the funds are deposited into the institution's bank account. Cash-basis accounting focuses exclusively on when cash is received or paid. It is plain that funds that have been deposited in an institution's bank account for the use of the institution have been received by that institution.

OIG Comments. The formula for the 90/10 revenue computation provides that funds used to satisfy tuition, fees, and other institutional charges are to be included in the computation. Until funds are posted to a student's account, the funds have not been used to satisfy tuition, fees, and other institutional charges nor may they be considered to be revenue generated from tuition, fees, and other institutional charges for students enrolled in eligible programs. The fact that funds have been transferred to an institution's account does not mean that those funds have been used for tuition, fees, and other institutional charges. Until the funds have been posted to a student's account, an institution cannot know what, if any, portion is cash basis revenue because some funds may be disbursed directly to the student for non-institutional expenses, and some of the remaining funds may be used to satisfy tuition, fees, and other institutional charges. In the case of ACT, some funds received were not disbursed at all.

In the preamble to the final regulations published on October 29, 1999, 64 Federal Register No. 209, 58610 (October 29, 1999 Preamble), the Department clarified that "the regulation applies to cash received used to satisfy tuition, fees and other institutional charges." Therefore, funds are to be received and used within the fiscal year in order to be included as 90/10 revenue. The receipt of cash is not revenue for 90/10 purposes until it is posted to student accounts and used to satisfy tuition, fees, and other institutional charges.

Our position is further supported by ACT's inadequate policies and procedures in place over the administration of Title IV funds during the audit period. As discussed in Finding 2 of this report, ACT breached its fiduciary responsibility regarding the use of Title IV funds by transferring Title IV funds to its operating account one day after drawing down the funds from the Department and not disbursing the funds to student accounts within three business days. In some instances, funds were not disbursed to student accounts at all. By basing its 90/10 calculation on the date funds are received, ACT would include funds in the calculation that have not been used to cover tuition fees, and other institutional charges.

Sallie Mae Loan Revenue

ACT Response. ACT utilized the CLASS software system for accounting for student aid funding, including Title IV funding, and maintaining records regarding student activity. The CLASS system provides a number of data fields to track information related to student accounts, including a "transaction date" and a "posting date." Under the CLASS system, the transaction date was entered on a student account only after ACT had received the funds with respect to that student. In most cases, such funds were received into the ACT bank account managed through the IEC corporate office so that, upon receipt, the corporate office personnel would notify ACT through a transmittal document that the funds had been received and instruct ACT to credit the student's account using the transmittal date as the transaction date.

With regard to the receipt of loan funds from Sallie Mae, the transaction date was supported by receipts for wired funds, which were dated on or before the transaction date for the affected students. The transaction date was entered into the CLASS system after the IEC corporate office or ACT personnel had confirmed that the applicable funds had been received into the ACT bank account and were available, without restriction, to pay the obligations of the student borrowers.

All funds are considered credited to the student's account as of the transaction date entered for those funds.

The audit report uses the posting date to determine when funds, including Sallie Mae loan funds, were received for purposes of the 90/10 Rule. The OIG only counted Sallie Mae loans in the 90/10 ratio if such loans had a posting date on or before October 31, 1999. This resulted in the exclusion of $246,684 in Sallie Mae loan funds for 26 students whose accounts had transaction dates prior to October 31, 1999, but posting dates on or after November 1, 1999. In the case of all 26 students, ACT had received $246,684 from Sallie Mae on or before the transaction date. These funds must be counted for a total of $785,346 in Sallie Mae loan funds in the school's 90/10 calculation for FY 1999.

OIG's use of the figure derived from the posting date rather than the transaction date is wrong as a matter of fact and law. The report would suggest that the transaction date is nothing but a prediction of the date that a transaction "should" occur. This is a fundamental misunderstanding, which ignores that ACT never determined and entered the transaction date for Sallie Mae loans into the CLASS system until such funds had been received into ACT's bank account. ACT treated, and continues to treat, the transaction date as the date that funds are credited to the student's account.

ACT treated the transaction date as the date that funds were credited to its student's accounts as a payment of the student's obligations. Under the Sallie Mae Loan Agreement, it is clear that Sallie Mae actually disbursed funds to the students (as identified by name and exact dollar amount on the wire transmittals) when it wired funds on behalf of those students to the ACT bank account. ACT then entered a transaction date on the student's account to reflect that the funds for that student had been received and credited as a payment on the student's account on or before such transaction date.

It is notable that 21 of the 26 loans with transaction dates prior to October 31, 1999, have a posting date of November 1, 1999. For these 21 loans totaling $218,895, ACT made the manual accounting entry that generated the posting date on November 1st, the first business day following the close of FY 1999. For the report to deny that these loans belong in FY 1999 is to suggest that this issue should be decided by the mechanical question of when certain entries were made in the CLASS system, rather than when the funds were actually received by ACT and credited by the school to the student's account to pay the student's charges.

<u>OIG Comments</u>. To be counted for 90/10 purposes, Title IV and non-Title IV funds must be used to satisfy tuition, fees, and other institutional charges. Funds cannot be considered used until they are posted to student accounts. Regardless of the transaction date information provided by ACT, funds cannot be included in the 90/10 revenue calculation until they have been used to satisfy tuition, fees, and other institutional charges.

Our analysis of the transaction date data revealed that the transaction dates were not verifiable. Our review of a random sample of 74 student files who received Title IV funds during academic years 1999-2000 or 2000-2001 revealed that the <u>transaction date data</u> showed that Title IV funds were disbursed to 18 student accounts greater than three days from the date the funds were drawn down. The number of days ranged from 4 to 368. In addition, the transaction date data showed that funds were disbursed to 11 students <u>before</u> the date the funds were drawn down. Therefore, we concluded that the transaction date data were not reliable for 90/10 computation purposes.

Since the posting date was automatically generated by the computer system and represented the date that the disbursements were actually credited to student accounts (and, therefore, used for the intended purpose), we concluded that the posting date data reflected the date that the disbursements occurred.

Regarding the exclusion of $246,684 in Sallie Mae loan funds for 26 students whose accounts had transaction dates prior to October 31, 1999, but posting dates on or after November 1, 1999, the regulations state that funds are to be included in the 90/10 revenue calculation in the fiscal year that the funds are used to satisfy tuition, fees, and other institutional charges. The treatment of such funds was addressed in the October 29, 1999 Preamble to the 64 Federal Register No. 209, 58610 (October 29, 1999). The preamble provided the following example for an institution whose fiscal year is a calendar year:

> On December 30, 1999, the institution disburses $100,000 of Title IV, HEA program funds to students on their accounts, and credit balances occur because the institution has not yet charged those accounts with related tuition and fees. On January 3, 2000, the institution charges tuition and fees to the students' accounts, and uses all of those previously disbursed funds to pay the students' tuition and fee charges. For purposes of the 90/10 formula in 600.5 (d)(1), none of the $100,000 would be included in the institution's 90/10 calculation for its 1999 fiscal year because none of the funds had been used for tuition, fees, and other institutional charges; all of the $100,000 would be included in the institution's 90/10 calculation for its 2000 fiscal year calculation, when the funds were used to satisfy tuition, fees, and other institutional charges.
>
> A similar result would apply if the institution drew down $100,000 of Title IV, HEA program funds from the Department on December 30, 1999, but did not pay those funds to students for institutional charges until January 3, 2000.

The Sallie Mae recourse loans made by ACT on the last day of the fiscal year for the full cost of tuition and fees closely resembled invalid institutional loans as outlined in Dear CPA Letter 99-02 (CPA-99-02).[3] Our analysis of the Sallie Mae recourse loans made to ACT students in FY's 1999 and 2000 revealed that if these loans had been institutional loans, they would not have been considered valid. In November 1999, the OIG issued Dear CPA Letter 99-02 outlining the following tests: Evaluate whether the institutional loans are routinely repaid and evaluate the timing of the loans. The Dear CPA Letter stated that an indication that institutional loans are routinely repaid is whether the default rate exceeds 15 percent; and an indication that

[3] CPA Letter 99-02 was written in response to Dear Partner Letter GEN 99-33 to provide guidance to auditors in evaluating the validity of institutional loans and scholarships. Dear Partner Letter GEN 99-33 established the Department's policy for accepting institutional loans and scholarships after the 1998 Reauthorization of the Higher Education Act until new regulations went into effect on July 1, 2000. CPA Letter 99-02 was developed in conjunction with and approved by the Department.

institutional loans may not be valid would be where the majority of the loans are made at the end of an institution's fiscal year rather than at recurring intervals that are related to the institution's enrollment cycle. The letter stated that, in general, institutional loans would typically be made around the time a student begins an academic year or new period of enrollment. We found that the large Sallie Mae loans made to students failed these tests.

- *Loan Repayment*
  During FY's 1999 and 2000, students did not routinely repay the large Sallie Mae recourse loans. Of the 83 students who received a Sallie Mae recourse loan for the full cost of tuition and fees in October 1999 or 2000, ACT repurchased 35 (42 percent) of these loans within the following two years because students defaulted on them.

- *Timing of Loans*
  During FY's 1999 and 2000, the majority of the Sallie Mae recourse loans were made in October, the end of the institution's fiscal year, rather than at recurring intervals related to the institutions enrollment cycles. Prior to October, ACT awarded very few Sallie Mae recourse loans and the amounts of the loans were not for the full cost of tuition and fees. We found that most Sallie Mae recourse loans made to students during October 1999 or 2000 were for a larger amount than during any other time during the fiscal year. We identified 83 Sallie Mae recourse loans that were made for the full costs of tuition and fees in October 1999 and 2000. Only 5 Sallie Mae recourse loans for the full cost of tuition and fees were made in months other than October.

As noted in the Other Matters section of this report, we reviewed the files of 61 of the 84 students who received large Sallie Mae recourse loans for the full cost of tuition and fees during FY's 1999, 2000, and 2001. Of the 61 student files reviewed:

- 53 students received cash payments (totaling $228,382) of the Sallie Mae loan proceeds.

- 40 students had Direct Loans prior to receiving the large Sallie Mae loans. Of these 40 students, 29 cancelled their Direct Loans or ACT repaid the Direct Loans when the students obtained the large Sallie Mae loans.

- 15 students were eligible for Direct Loans, but took Sallie Mae loans instead.

- 9 Sallie Mae loans were cancelled by ACT during the first month of the next fiscal year.

- 35 Sallie Mae loans were repurchased by ACT within the following two years because the students defaulted on the loans.

Regarding the 26 Sallie Mae loans with posting dates after October 31, 1999, 17 of these students already had Direct Loans and another 4 students had Pell grants. For these 21 students who already had either Direct Loans or Pell grants, the Sallie Mae loans created credit balances in the student accounts. Therefore, it is questionable whether these students needed the Sallie Mae loans.

Sallie Mae Escrow Adjustment

ACT Response. In July 1999, ACT's parent corporation, IEC, entered into an agreement with an affiliate of Sallie Mae and Mid-City National Bank under which Sallie Mae agreed to make privately funded loans to students who would otherwise not qualify for such loans due to their credit history or other factors. Under the agreement, IEC agreed to establish and maintain an escrow account to be equal to 30 percent of the original principal balance of each loan made by Sallie Mae to ACT students. IEC had the option of funding the escrow account through its own payments or agreeing that Sallie Mae could withhold funds for that purpose from new loan disbursements. IEC further agreed to credit the student borrower with 100 percent of the loan amount for payment of tuition and fees or other costs of education reflecting that these were loans from Sallie Mae to the students for the benefit of the students.

The report adjusts the Sallie Mae loans included in the 90/10 ratio by reducing the total loan principal by the 30 percent that would be paid into the escrow account. Thus, the OIG input its own figure of $161,599 (representing 30 percent of the loan amount of $538,662) even though actual cash transactions in the escrow account were significantly less. As of October 31, 1999, ACT or Sallie Mae had deposited the sum of $41,259 in the escrow account. This figure is slightly higher than the figure cited in the report due to the discovery of one additional payment to the escrow account. Subsequently, in school FY 2000, ACT made payments to bring the escrow account up to the customary 30 percent coverage.

OIG Comments. ACT provided documentation to support that $41,259 was placed in the escrow account during FY 1999. Since most of the Sallie Mae loans were made on October 29, 1999, we agree that it is reasonable that funds would not have been deposited in the escrow account for these loans until November (i.e., the beginning of the next fiscal year). We agree with this treatment and have used the $41,259 figure in our 90/10 revenue calculation (see Attachment A).

Although we agree to this treatment of the escrow for purposes of the 90/10 revenue calculation, it should be noted that IEC had an agreement with Sallie Mae Financial Corporation to allow IEC to defer replenishment of the reserve account held with Sallie Mae until the first month of the fiscal year. In September 2001, the Sallie Mae Financial Corporation and IEC mutually agreed to allow IEC "to defer replenish the reserve accounts for the months of August and September 2001 . . . and replenish the reserve accounts after October 31, 2001, but prior to November 10, 2001." According to the letter, this was done to help IEC "satisfy U.S. Department of Education regulation generally referred to as the 90/10 Rule." By deferring the replenishment of the escrow account, ACT reported no repurchases during these months, thus artificially inflating the non-Title IV cash portion of the calculation. In addition, ACT deferred Title IV draws during the last months of the fiscal year until the first month of the next fiscal year to help meet the 90/10 eligibility requirement.

Sallie Mae Credit Balance Adjustment

ACT Response. The OIG significantly reduced the value of the Sallie Mae loans received by ACT by subtracting for credit balances on student accounts. The report reduces the value of the Sallie Mae loan principal based on credit balances in the amount of $148,065. That figure represents a 30 percent reduction of the $211,521 in credit balances on the student accounts. The OIG made the 30 percent adjustment since the OIG also reduced the Sallie Mae loan principal by 30 percent based on the OIG's interpretation of the requirements of the escrow account. The OIG adjustment for credit balances is based entirely on credit balances recorded on students' accounts, without regard to when those credit balances were paid.

As of FY 1999, the Department had not issued any regulatory guidance specifically addressing the treatment of credit balances in the 90/10 calculation. While the Secretary issued guidance in the Federal Register of October 29, 1999, indicating that funds held as credit balances generally are not counted in an institution's 90/10 calculation, that guidance was published on the last business day of the school's FY 1999, in connection with regulatory revisions that did not take effect until July 1, 2000. As a result, the exclusion of credit balances from the 90/10 calculation was not expressly called for until FY 2000.

OIG Comments. We identified $211,521 in credit balance adjustments during school FY 1999. We initially reduced this amount by 30 percent in the draft report to allow for the Sallie Mae escrow account. However, since we agree to limit the Sallie Mae escrow account adjustment to the amount deposited in escrow during FY 1999 ($41,259), we used the $211,521 credit balance in the final report (see Attachment A).

The regulations provide that credit balances occur whenever an institution disburses Title IV funds by crediting a student's account and the total amount of all Title IV funds credited exceeds the amount of tuition and fees, room and board, and other authorized charges (34 CFR 668.164(e)). In other words, a credit balance is money credited to a student's account that is not being used to pay for tuition, fees, and other institutional charges. At the point that there is a credit balance, the funds have not been used for tuition, fees, and other institutional charges and cannot be used for 90/10 purposes. The preamble to the final rule in the October 29, 1999, Preamble, states "In general, funds held as credit balances in institutional accounts do not get counted in the 90/10 formula in 600.5(d)(1)."

Sale of Institutional Retail Installment Contracts

ACT Response. The sale of institutional retail installment contracts (RIC) on October 29, 1999, resulted in the receipt of an additional $90,295 in non-Title IV funds in FY 1999. This sale transaction was mistakenly overlooked and the sale proceeds were not included in the 90/10 calculation as originally performed by ACT and its auditor. ACT discovered the sale documents in preparing this response and presents them to the OIG for the first time in connection with this response. This $90,295 was the payment received from an independent third party, as demonstrated by the wire transfer records and purchase agreement. The schedule to the purchase agreement identifies the student loans that were sold and generating revenue received by ACT in FY 1999.

OIG Comments. ACT provided adequate documentation to support the receipt of an additional $90,295 in non-Title IV funds for the sale of retail installment contracts (RIC) on October 29, 1999. We included this sale in our revised 90/10 revenue calculation. During the audit, ACT provided documentation to support $22,375.26. Therefore, we adjusted the RIC sales to include the amounts supported ($112,670.26). See Attachment A.

Finding No. 2 – ACT Breached Its Fiduciary Responsibility Regarding the Use of Title IV Funds

ACT did not maintain Title IV funds in an interest-bearing account identified as containing Federal funds. It was IEC policy to transfer Title IV funds to its operating account one day after drawing down the funds from the Department. ACT did not disburse Title IV financial aid funds to student accounts within three business days following the date the institution received the funds, and in some cases the funds were not disbursed at all. As a result, not all Title IV funds were used for their intended purpose. This failure to assure that Title IV funds were used for their intended purpose placed ACT in violation of its fiduciary responsibility.

The regulations at 34 C.F.R. § 668.82(a), (b)(1), and (c) state that an institution:

> must at all times act with the competency and integrity necessary to qualify as a fiduciary . . . .
>
> In the capacity of a fiduciary . . . A participating institution is subject to the highest standard of care and diligence in administering the programs and in accounting to the Secretary for the funds received under those programs . . . .
>
> The failure of a participating institution . . . to administer a Title IV, HEA program, or to account for the funds that the institution . . . receives under that program, in accordance with the highest standard of care and diligence required of a fiduciary, constitutes grounds for . . . an emergency action against the institution, a fine on the institution, or the limitation, suspension, or termination of the institution's participation in that program . . . .

The regulations at 34 C.F.R § 668.161(b) state that "funds received by an institution under the [T]itle IV, HEA programs are held in trust for the intended student beneficiaries and the Secretary . . . . The institution, as a trustee of Federal funds, may not use or hypothecate (i.e., use as collateral) [T]itle IV, HEA program funds for any other purpose."

The regulations at 34 C.F.R § 668.163(c)(2) state that for institutions drawing down $3 million in the previous year "an institution must maintain Direct Loan, Federal Pell Grant, FSEOG, and FWS program funds in an interest-bearing bank account . . . ." The regulations at 34 C.F.R. § 668.166(a) provide that institutions are to disburse Title IV funds to students or credit their accounts within three business days.

An analysis of ACT's Direct Loan Federal Funds accounts from 1998 through 2000 revealed that Direct Loan funds drawn from the Department were wired to the Direct Loan Federal Funds account. However, these funds were transferred from the Direct Loan Federal Funds account to a non-interest-bearing operating account the following day. IEC staff would then inform the applicable ACT campuses that the funds had arrived and direct them to disburse the funds to the appropriate student accounts.

Title IV funds are to be maintained in a Federal Funds account until disbursed for their intended purpose. The funds are to be held in trust for the intended student beneficiary and cannot be used for any other purpose. An institution has not used Title IV funds for their intended purpose until it has disbursed the funds to the intended student beneficiaries. IEC's practice of transferring Title IV funds into its operating account within one day of receipt without disbursing the funds to students breached its fiduciary responsibility to the Secretary.

IEC could not account for all of the funds that it drew down from the Department. We compared the total amount of Title IV funds drawn down from the Department's GAPS system to the total amount of Title IV funds posted to student accounts per ACT's CLASS system for school FY's 1999, 2000, and 2001. The tables below illustrate that the Title IV drawdowns (less refunds) exceeded the amounts posted to student accounts by $994,619 for FY's 1999 through 2001.

Table 2.1 - Direct Loan Drawdowns vs. Amounts Posted to Student Accounts

Fiscal Year	GAPS	CLASS	Difference
1999	$4,674,687	$4,493,067	$181,620
2000	5,201,173	4,536,704	664,469
2001	6,812,068	6,879,979	(67,911)
TOTALS	$16,687,928	$15,909,750	**$778,178**

Table 2.2 - Pell Grant Drawdowns vs. Amounts Posted to Student Accounts

Fiscal Year	GAPS	CLASS	Difference
1999	$1,563,993	$1,531,801	$ 32,192
2000	2,075,046	1,930,274	144,772
2001	2,808,319	2,859,397	(51,078)
TOTALS	$6,447,358	$6,321,472	**$125,886**

Table 2.3 – FSEOG Drawdowns vs. Amounts Posted to Student Accounts

Fiscal Year	GAPS	CLASS	Difference
1999	$ 31,748	$ 9,945	$21,803
2000	75,128	108,954	(33,826)
2001	133,922	31,344	102,578
TOTALS	$240,798	$150,243	**$90,555**

On October 31, 2001, ACT/IEC returned $900,000 in Direct Loan funds to the Department. ACT/IEC also returned $265,000 in Pell grant funds to the Department on November 14, 2001. According to IEC officials, the returned funds represented excess cash accumulated during FY's 1999 and 2000.

ACT did not disburse Title IV funds to students within three business days following the date the institution received the funds. We reviewed a random sample of 74 files of students who received Title IV funds during academic years 1999-2000 or 2000-2001 (July 1, 1999, through June 30, 2001). ACT failed to post Title IV funds to student accounts within allowable time periods for about two-thirds of the files reviewed.

Of the 74 files reviewed, 52 student accounts were not credited with Title IV funds within three business days of the date that the funds were drawn per the support provided for the drawdowns. We identified 176 disbursements that were not posted to the 52 student accounts within three business days (per ACT's accounting system post date). ACT officials were unable to provide names of alternative students who received the funds. Table 2.4 below illustrates the number of lapsed days for the 52 student accounts reviewed (176 disbursements).

Table 2.4 – Disbursement Elapsed Days for the 52 Students Whose Accounts Were Not Credited Within Three Business Days of Drawdown of Funds

Elapsed Days	Disbursements
4-5	51
6-10	46
11-50	55
51-100	9
101-300	4
301-500	8
501-650	3
Total	176

ACT had no written policies and procedures over the draw down and disbursement of Title IV funds. ACT also experienced a high turnover in financial aid personnel and the current employees could not explain the process used for drawing down and disbursing Title IV funds during award years 1998 or 1999. In April 2000, ACT signed a contract with Global Financial Aid Services (Global) to perform certain aspects of the draw down and disbursement of Title IV funds as a third-party servicer.

During the audit exit conference, ACT/IEC officials agreed that there were two issues in this finding that needed to be addressed: (1) Title IV funds not kept in an interest bearing account until disbursed to student accounts and (2) Title IV funds not being disbursed to student accounts within three business days. The IEC Vice President of Student Financial Services said ACT got into the situation of not posting large amounts of Title IV funds to student accounts within the required timeframe because of turnover in personnel. In February 2001, ACT began trying to reconcile the Direct Loan and Pell accounts. The Direct Loan process involved matching students for which ACT had a valid promissory note to Title IV draw downs made and posted. The result of the Direct Loan and Pell reviews was the return of $900,000 of Direct Loan funds and $265,000 of Pell funds to the Department of Education.

RECOMMENDATIONS

We recommend that the Chief Operating Officer for Federal Student Aid:

2.1 Place ACT on the reimbursement method of payment for all the Title IV programs.

2.2 Require ACT to maintain Title IV fund drawdowns in an interest-bearing Federal Fund account until the funds are disbursed to students.

2.3 Require ACT to establish policies, procedures, and management controls to ensure that Title IV funds are disbursed to student accounts within three business days following the date the funds are received.

2.4 Take appropriate action under 34 C.F.R. Part 668, Subpart G to fine, limit, suspend, or terminate the participation of ACT in the Title IV programs as a result of ACT's breach of fiduciary responsibility.

ACT RESPONSE

In its written response to the draft report (see Attachment B), ACT agreed that for the period covered by the audit, it did not consistently disburse Title IV funds to students in accordance with all applicable Departmental requirements. During award year 2000-2001 to present, ACT contends that it maintained Title IV funds in bank accounts identified as containing Federal funds. However, these Federal funds accounts were not interest bearing accounts because ACT determined that the interest that would be earned on the funds in the accounts would be less than $250 per year. Regulations do not require institutions to maintain Title IV funds in an interest-bearing account if the institution will not earn over $250 during the award year.

It was ACT's practice during the years covered by the audit (school years 1999, 2000, and 2001) to transfer the Title IV funds it received out of the Federal funds account and into its operating account approximately one day after their receipt from the Department. ACT did this because a predominant number of ACT students use all of the Title IV funds awarded to them to pay institutional charges (i.e., tuition, fees, books, and related charges). It was ACT's intent that, immediately upon transfer of the funds to the institutional operating account, it would credit the funds to the student's tuition accounts. Unfortunately, during the period covered by the audit, this did not always happen on a consistent basis, and funds were not consistently credited to student's accounts within three business days. ACT conceded that practices like this that were initiated by the prior management of ACT's parent company were sometimes too informal and, therefore, not consistent with applicable Federal regulations.

ACT has made several significant changes to institutional policies and operations to address this problem. In 2000, ACT engaged the services of Global Financial Aid Services, an experienced third-party servicer, to handle key aspects of ACT's drawdown and disbursement of Title IV funds. ACT has dramatically reduced the time lapse between the date Title IV funds are drawn down and the date those funds are credited to students' accounts.

The audit report describes past procedures and a problem that went back as far as five years. ACT has taken numerous steps to revise it practices, including the retention of a respected third-party servicer, Global Financial Aid Services, to help administer its Title IV funds appropriately and to help ensure these past practices will not continue. For those reasons, ACT does not believe that it should be placed on reimbursement, or that its Title IV participation should be limited, suspended, or terminated.

OIG COMMENTS

ACT agreed that for the period covered by this audit, it did not consistently disburse Title IV funds to students in accordance with applicable regulations. ACT's response that it did not deposit Title IV funds into an interest bearing account because the amount of interest earned would be less than $250 annually does not address the primary violation. ACT's breach of its fiduciary responsibility is the fact that ACT did not maintain the Title IV funds in the Federal Funds account until the funds were disbursed to student accounts. The transfer of Title IV funds to the operating account one day after the funds were drawn down did not necessarily mean the funds were posted to student accounts.

Furthermore, under the system in place at the time of our audit, ACT's use of the CLASS system transaction date data made it appear that ACT was in compliance with the requirement to disburse Title IV funds to students within three business days when in many instances it did not. To be in compliance with regulations, it would be necessary for the transaction date to represent the date that funds were actually posted to student accounts.

The new procedure described by ACT for Pell and Direct Loan disbursements will not resolve the 90/10 revenue problems noted in this report unless (1) the transaction date and posting date are the same as the date the funds are credited to student accounts and (2) the funds are disbursed to students within three business days from the date of drawdown. We did not change our findings and recommendations regarding ACT's breach of its fiduciary responsibilities.

Finding No. 3 – ACT Improperly Disbursed Title IV Funds to Ineligible Students

ACT improperly disbursed Title IV funds totaling $67,744 to (1) seven students more than 90 days after their last date of attendance, (2) three students who had withdrawn from school, and (3) four students who did not pass the ability-to-benefit test.

The regulations at 34 C.F.R. § 668.164(g)(2)(ii)(A) and (3) provide that:

> An institution may not make a late or subsequent disbursement of a Direct Subsidized or Direct Unsubsidized loan unless the student has graduated or successfully completed the period for which the loan was intended . . . .
>
> If a student or parent borrower qualifies for a late disbursement . . . the institution . . . [m]ay make that late disbursement of [T]itle IV, HEA program funds only if the funds are used to pay for educational costs that the

institution determines the student incurred in the period in which the student was enrolled and eligible; and . . . [m]ust make the late disbursement no later than 90 days after the date that student becomes ineligible . . . .

The regulations at 34 C.F.R. § 668.24(c)(1)(iii) require "[t]he records that an institution must maintain . . . include but are not limited to--Documentation of each student's . . . eligibility for [T]itle IV, HEA program funds . . . ."

The regulations at 34 C.F.R. § 668.32(e)(2) state that "[a] student is eligible to receive [T]itle IV, HEA program assistance if the student – [h]as obtained within 12 months before the date the student initially receives [T]itle IV, HEA program assistance, a passing score specified by the Secretary on an independently administered test . . . ."

ACT improperly disbursed Title IV funds totaling $25,587 to eight students more than 90 days after their last date of attendance. ACT returned to the Department $2,141 disbursed to one of these students, leaving a balance owed of $23,446. ACT also made second Direct Loan disbursements totaling $4,688 to three students after their last date of attendance even though the students withdrew before the end of the payment period.

ACT did not always maintain documentation of the Wonderlic Ability-to- Benefit (ATB) test scores in student files. A comparison of the Department's National Student Loan Data System (NSLDS) and Wonderlic's ATB database identified 11 students who received student financial aid, but did not pass the Wonderlic ATB test. A review of these 11 student files revealed that four files did not contain adequate documentation to establish eligibility to receive Title IV funds. As a result, $39,610 was disbursed to four ineligible students.

ACT officials stated that the institution had a high turnover in staff. We concluded that this contributed to ACT's difficulty in processing financial transactions accurately, timely, and in accordance with regulations. We also noted that there was confusion among financial aid personnel regarding whose responsibility it was to post Title IV funds to student accounts once the campus was notified that the funds had arrived.

RECOMMENDATIONS

We recommend that the Chief Operating Officer of Federal Student Aid require ACT to:

3.1 Return $67,744 of Title IV funds that were improperly disbursed.[4]

3.2 Address confusion among financial aid personnel regarding their responsibilities to ensure that ineligible students do not receive Title IV disbursements.

[4] It should be noted that $3,852 of the $67,744 was disbursed during school FY 2000. Therefore, if it is determined that ACT must return the $7.4 million in Title IV funds that it received during school FY 2000 as a result of Finding No. 1, the $3,852 should be deducted from the $67,744 (i.e., the $3,852 is included in the $7.4 million).

ACT RESPONSE

The ACT written response (see Attachment B) provided additional information for each of the students identified in the draft report as receiving improper Title IV disbursements. The response also stated that ACT had implemented various new procedures and had provided additional training to its staff to ensure that Title IV funds are not disbursed to ineligible students. ACT is discontinuing use of ability-to-benefit testing for admitting new students. Effective June 1, 2003, new applicants to ACT will only be admitted if they have a high school diploma or GED certificate.

OIG COMMENTS

Based on the additional information provided by ACT in its response to the draft report, we adjusted the finding to include eight students (down from nine) who received Title IV funds more than 90 days after their last date of attendance; three students (up from two) who received Title IV funds after their last date of attendance even though the students withdrew before the end of the payment period; and four students (down from five) who did not have passing ATB test scores. The one student file that was missing was provided for review. Based on the additional information provided, we reduced the total amount of improperly disbursed Title IV funds to $67,744 (from $82,832).

Finding No. 4 – ACT Did Not Reconcile Direct Loan Funds

ACT did not reconcile its 1998-1999 or 1999-2000 Direct Loan awards on a monthly basis. ACT/IEC officials stated that these awards were not reconciled due to high staff turnover and improperly trained personnel. Because the school's records do not match the Department's records, the Department cannot account for the Direct Loan funds or identify potential problems with timely disbursements or excess cash.

The regulations at 34 C.F.R. § 685.102(b)(3) for an origination option 2 school such as ACT states that the school "reconciles on a monthly basis." Direct Loan Bulletin-97-49 provides that "Each academic year will be closed on July 31st of the year following the academic year."

The regulations at 34 C.F.R. § 685.402(c)(2) state:

> The Secretary may require a school to change origination status if the Secretary determines that such a change is necessary to ensure program integrity or if the school fails to meet the criteria and performance standards established by the Secretary, including but not limited to . . . the timely submission of completed and signed promissory notes and accurate origination and disbursement records, and the successful completion of reconciliation on a monthly basis.

We reviewed a judgment sample of six months each of Direct Loan Student Account Summary (DLSAS) reports for the 1998-1999 and 1999-2000 award years to determine whether ACT reconciled its Direct Loan awards on a monthly basis. The DLSAS reports showed that ACT carried an ending cash balance at the end of 10 of the 12 months reviewed. ACT also carried an ending cash balance and unbooked loans after the close of the 1998-1999 and 1999-2000 academic years.

ACT's failure to reconcile its Direct Loan awards on a monthly basis contributed to the unaccounted for Direct Loan funds that were not returned to the Department in a timely manner. We reviewed ACT's bank statements, GAPS activity reports, and student ledgers for a judgment sample of three months each for award years 1998-1999, 1999-2000, and 2000-2001 to determine whether funds drawn down from GAPS were disbursed to student accounts. We noted a significant difference between the amount of funds drawn from GAPS and the amount of funds disbursed to student accounts in seven of the nine months reviewed. These funds represented unaccounted for loan funds in the ACT operating account.

IEC officials were attempting to reconcile these awards at the time of the audit. On October 31, 2001, IEC returned to the Department $900,000 of unaccounted for funds from Direct Loan award years 1998-1999 and 1999-2000. According to IEC officials, $150,000 was from award year 1998-1999 and $750,000 was from award year 1999-2000.[5]

IEC signed a contract with Global Financial Aid Services (Global) in April 2000 for Global to perform ACT's 2000-2001 Direct Loan reconciliation. Global began handling the reconciliation of ACT's 2000-2001 Direct Loans for the month ended September 30, 2000. A limited review of Global revealed that it had policies and procedures in place for reconciling ACT's 2000-2001 Direct Loans on a monthly basis. Our analysis of a three-month sample of DLSAS reports revealed that Global was following its procedures and reconciling ACT's 2000-2001 Direct Loans on a monthly basis.

RECOMMENDATION

We recommend that the Chief Operating Officer for Federal Student Aid require ACT to:

4.1 Train personnel in the reconciliation requirements of the Direct Loan program.

4.2 Monitor its third-party servicer's performance to ensure continued compliance with program requirements.

ACT RESPONSE

ACT agreed that it did not reconcile its Direct Loan accounts on a monthly basis during 1988-1999 and 1999-2000. However, subsequent to that time ACT initiated a reconciliation of its

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[5] An additional $47,237 of excess cash was due for the 1998-1999 Direct Loan award. Subsequent to the completion of our audit work, the Division Director of Case Management and Oversight issued a Final Program Review Determination on January 4, 2002, requiring ACT to return $52,267, which included an additional excess cash balance of $47,237 for the 1998-1999 Direct Loan award year plus accrued interest of $5,030. The school appealed this determination, and the Department subsequently agreed to allow the $47,237 of excess cash be paid by offset against money due back to the institution from the Direct Loan program for the 1997-1998 award year. A check was paid for the $5,030 of accrued interest.

Direct Loan funds. As a result of that reconciliation, ACT returned excess cash funds to the Department, as acknowledged in the audit report. In April 2000, ACT engaged Global Financial Aid Services to perform a variety of Title IV cash management functions. One of the services Global performs on behalf of ACT is the reconciliation of Direct Loan transactions. Global began conducting complete monthly reconciliation of Direct Loans at the beginning of the 2000-2001 school year. ACT personnel are now fully aware of the monthly reconciliation requirements and the Global staff performing the reconciliation is fully trained, experienced, and capable to perform those duties.

OIG COMMENTS

ACT agreed that it did not always reconcile Direct Loan funds in accordance with Departmental requirements. Although ACT engaged Global Financial Aid Services to perform their reconciliation of Direct Loan funds, ACT remains the responsible party regarding compliance with Direct Loan program requirements. Our limited review of Global revealed that it had policies and procedures in place for reconciling Direct Loans on a monthly basis; however, we did not make a determination as to whether the reconciliation was timely and accurate. We did not change our findings and recommendations regarding Direct Loan reconciliation.

Finding No. 5 – ACT Failed to Properly Calculate or Make Refunds For Students Who Withdrew

ACT failed to make refunds for ten students and incorrectly calculated refunds for two students in our sample who withdrew during academic years 1999-2000 and 2000-2001. As a result, ACT owes the Department $9,619 for refunds not made or made in the incorrect amount.

Institutions are required to calculate returns of Title IV funds for students who withdraw according to the procedures in 34 C.F.R. § 668.22 (2000). Amended regulations to implement the return of Title IV requirements of the Higher Education Amendments of 1998 were published in the Federal Register on November 1, 1999. Institutions were not required to implement these new requirements until October 7, 2000, although institutions could choose to implement them earlier. ACT did not choose early implementation. We used the appropriate refund calculation depending on when the refund was made.

ACT did not always calculate refunds correctly or make the refunds. A review of the files of 23 randomly selected students who withdrew from ACT's Atlanta campus during the 2000-2001 school year revealed that two refunds were not made at all and one refund made was calculated incorrectly.

We also reviewed refunds as part of our student eligibility file review. Of the 74 files reviewed of students who received Title IV funds during academic years 1999-2000 and 2000-2001, 28 students withdrew and required a refund calculation. Of these 28 students, eight refunds were not made and one was made, but calculated incorrectly.

Of the 51 (23 + 28) student files reviewed that required refund calculations, ACT failed to make refunds for ten students and two refunds were made, but calculated incorrectly. As a result of its failure to correctly calculate and/or make refunds for these12 students, ACT owes the Department $9,619.

ACT has a history of refund problems. ACT's FY 1999 and FY 2000 compliance audits contained findings pertaining to untimely refunds and the failure to make refunds.[6] To resolve the FY 1999 refund finding, the Office of Federal Student Aid required ACT to conduct a full file review to identify all late refunds. This file review indicated that of 152 refunds, 58 were paid late (38 percent), and of the $239,516 of refunds paid, $104,152 were paid late (44 percent). The Office of Federal Student Aid also required ACT to conduct a full file review to resolve the FY 2000 refund findings. The compliance audit identified refunds totaling $24,278 that had not been paid and $11,114 in refunds that were paid late. The full review identified refunds totaling $112,884 that had not been paid for the FY 2000 award year. The Department requested and received a letter of credit for $3.5 million from IEC relating to ACT's refund issues.

During the audit exit conference, IEC's Vice President of Student Financial Services stated that ACT has historically had a problem with refunds. The officials said a new system to calculate refunds was implemented in July 2001 to resolve this problem. We did not review this system.

RECOMMENDATIONS

We recommend that the Chief Operating Officer for Federal Student Aid:

5.1 Require ACT to refund to the Department $9,619 (less $3,255 paid subsequent to the issuance of the draft audit report) for refunds not made or made in the incorrect amount.

5.2 Require ACT to implement policies, procedures, and management controls to ensure the accurate calculation of refunds and the timely return of such refunds to the Department.

5.3 Take appropriate action under 34 C.F.R. Part 668, Subpart G to fine, limit, suspend, or terminate the participation of ACT in the Title IV programs as a result of ACT's continued failure to make refunds.

ACT RESPONSE

ACT provided additional information for each of the students cited in this finding. As a result of its recalculations for these students, ACT believes that the correct amount of additional refunds due is $3,255 for four students, which ACT fully paid prior to submitting its written response to the report. The ACT response also stated that the audit report notes that ACT had late and unmade refunds in the past, facts that ACT readily admit. ACT performed extensive file reviews over a period of several years, under the direction of the Department's Case Management [and Oversight] Team, to identify additional refunds that were not paid correctly and timely. ACT paid all additional refund amounts identified by those file reviews, and the Case Management Team closed the compliance reviews for those years.

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[6] The Office of Federal Student Aid also requested ACT to conduct a full file review for its fiscal year ending October 31, 2001, and for the period November 1, 2001, through December 31, 2001.

ACT's independent auditor's Title IV compliance attestation report for school FY 2000 identified only one late refund and no unmade refunds in its audit sample. Therefore, ACT believes that the refund problem is a problem of the past that has been cured. ACT developed and now has in place detailed policies and procedures for ensuring refunds are correctly and timely made. ACT believes that no additional adverse action against it is warranted, and requested that the recommendation to limit, suspend, or terminate ACT's participation in Title IV programs due to its failure to make refunds be removed from the final report.

OIG COMMENTS

Based on the additional information provided by ACT in its response to the draft report, we adjusted the finding to show that ACT failed to make refunds for ten students (down from eleven) totaling $9,042 and incorrectly calculated and made refunds for two students totaling $577. We also reduced the total amount of refunds due to $9,619 (from $10,112). We noted that ACT returned some of the recommended recoveries subsequent to issuing the draft audit report; therefore, we amended the amount to be recovered in Recommendation 5.1. Given ACT's history of refund problems, we did not change Recommendation 5.3.

Finding No. 6– ACT Did Not Demonstrate Administrative Capability

As discussed in Findings 1 through 5 above, ACT had significant problems affecting its ability to administer the Title IV programs. There was a high turnover of financial aid staff and a lack of management controls over program operations. As a result, ACT did not meet the administrative capability standards required to participate in the Title IV programs.

In order to continue participation in the Title IV programs, an institution must demonstrate that it:

> is capable of adequately administering that program under each of the standards established in this section. The Secretary considers an institution to have that administrative capability if the institution--Administers the Title IV, HEA programs in accordance with all statutory provisions of or applicable to Title IV of the HEA, all applicable regulatory provisions prescribed under that statutory authority, and all applicable special arrangements, agreements, and limitations entered into under the authority of statutes applicable to Title IV of HEA. [34 C.F.R. § 668.16]

Among the factors in 34 C.F.R. § 668.16 that should be considered in evaluating administrative capability are whether the institution:

> (a) Administers the Title IV, HEA program in accordance with all statutory provisions of or applicable to Title IV of the HEA, [and] all applicable regulatory provisions prescribed under that statutory authority . . .
> (c) Administers the Title IV, HEA programs with adequate checks and balances in its system of internal control . . .
> (d) Establishes and maintains all required records . . .

> (j) Shows no evidence of significant problems that affect the institution's ability to administer the Title IV programs that are identified by oversight agencies . . .
> (n) Does not otherwise appear to lack the ability to administer the Title IV programs competently . . . .

ACT did not administer the Title IV programs in accordance with all statutory and regulatory requirements when it failed the 90/10 revenue requirement; breached its fiduciary responsibility to the Secretary by using Title IV funds for other than their intended purpose; improperly disbursed Title IV funds to ineligible students; failed to reconcile its Direct Loan accounts with the Department; failed to make all required refunds; and failed to calculate refunds correctly. We attributed these problems to a lack of adequate accounting and management controls and a high turnover of financial aid staff. As a result, ACT did not meet the administrative capability standards required to participate in the Title IV programs.

RECOMMENDATION

We recommend that the Chief Operating Officer of Federal Student Aid:

6.1 Take appropriate action under 34 C.F.R. Part 668, Subpart G to fine, limit, suspend, or terminate the participation of ACT in the Title IV programs as a result of ACT's lack of administrative capability.

ACT RESPONSE

ACT stated that while it acknowledges that it had certain administrative and cash management problems in the past, it has also tried to demonstrate that it has devoted extensive attention and resources to correcting these problems. The problems identified in the audit report have been addressed and have been either completely or largely corrected. ACT addressed its past high turnover rate for financial aid staff by bringing in Global Financial Aid Services to perform many of the financial aid functions and by increasing training of its own financial aid employees. ACT's annual compliance audits show a distinct improvement in the magnitude and type of findings identified. ACT's most recent audits show marked improvement and a greatly reduced error rate, further attesting to its current administrative capability. Based on the corrective actions taken to address the issues identified in the report, and its current capabilities and processes, ACT does not believe that it should be limited, suspended, or terminated from future participation in the Title IV programs.

OIG COMMENTS

ACT agreed that during the period covered by this audit it did not always administer the Title IV programs in accordance with Departmental requirements regarding the drawdown and disbursement of Title IV funds to students; disburse Title IV funds to eligible students; reconcile Direct Loan funds on a monthly basis; and make refunds to students who withdrew. Therefore, ACT did not demonstrate administrative capability to administer the Title IV programs. We did not change our findings and recommendations regarding administrative capability. ACT stated that it plans to continue using the CLASS system transaction date data to compute 90/10 revenue. Since the transaction date data entered by ACT during the period of this audit was not reliable to determine when Title IV funds were disbursed to student accounts, the continued use of transaction date data in the same manner will not resolve the problem of inaccurate 90/10 revenue calculations. The 90/10 revenue computation will only be corrected if ACT changes its methodology for entering transaction date data whereby the date that Title IV funds are credited to student accounts is the same date as the posting date data.

OTHER MATTERS

To meet the 90/10 Rule requirement, it was IEC policy to maximize non-Title IV revenues near the end of the fiscal year. ACT did this, in part, by delaying the draw down of Title IV funds during the last months of the fiscal year until the next fiscal year, and by encouraging students to obtain Sallie Mae recourse loans during the last month of the fiscal year. In October 1999, 2000, and 2001, 84 students obtained Sallie Mae recourse loans for the full cost of tuition and fees (ranging from $9,995 to $11,895). Sallie Mae recourse loans for these amounts were rarely made during other months of the fiscal year.

We reviewed the files of 61 of the 84 students that obtained large Sallie Mae recourse loans. We found that 15 of the 61 students were eligible for Direct Loans, but ACT encouraged them to obtain a Sallie Mae recourse loan instead. Forty of the 61 students had a Direct Loan at the time they obtained the Sallie Mae loan. The Direct Loans for 29 of these 40 students were cancelled or repaid by ACT when the students obtained the Sallie Mae loans. The remaining 11 students kept both the Direct Loan and the Sallie Mae loan. The Direct Loans had an interest rate of 8.25 percent while the Sallie Mae loans had interest rates ranging from 14.63 to 15.94 percent. In addition to the lower interest rate, there were other benefits to Direct Loan such as deferment options and grace periods.

We also noted that ACT cancelled and returned 9 of the Sallie Mae loans during the first month of the next fiscal year (November 1999 and 2000, respectively). We also found that ACT repurchased 35 of the loans within the following two years because students defaulted on them. The IEC/ACT policy suggests that students were encouraged to obtain the large Sallie Mae loans to help ACT meet the 90/10 Rule.

BACKGROUND

Advanced Career Training Institute (ACT), founded in 1975, is a two-year proprietary institution with campuses in Atlanta and Riverdale, GA, and Jacksonville, FL. ACT offers vocational training in the following areas: Networking Technology, Dental Assistant, Medical Assistant, and Business Office Administration. ACT was accredited by the Accrediting Council for Continuing Education & Training and offered a degree in each vocational training program. ACT is owned by International Education Corporation, Inc. (IEC), located in Irvine, CA.

During school FY's 1999 through 2001, ACT participated in the William D. Ford Direct Loan Program, the Federal Pell Grant Program, the Federal Supplemental Educational Opportunity Grant Program (FSEOG), and the Federal Work Study (FWS) Program. According to GAPS, ACT drew down $23.5 million from the William D. Ford Direct Loan, Pell Grant, FSEOG, and Federal Work Study programs during FY's 1999, 2000, and 2001.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our audit objective was to determine whether ACT administered the student financial assistance programs in accordance with Title IV of the Higher Education Act of 1965, as amended, and applicable regulations. Specifically, we reviewed ACT's compliance with the requirements for (1) institutional eligibility, including the 90/10 Rule, accreditation, and State licensing, (2) cash management, (3) Direct Loan reconciliation, (4) refunds and the return of Title IV funds, (5) student eligibility, (6) program length, and (7) commissioned sales. Audit coverage included award years 1998-1999, 1999-2000, and 2000-2001. For purposes of the 90/10 revenue calculation and cash management review, audit coverage included school FY's 1999 through 2001. For program length, audit coverage included school FY 2001.

We accomplished these objectives by reviewing the HEA, regulations, and policies applicable to the Title IV programs. We interviewed officials representing ACT's Atlanta, Riverdale, and Jacksonville campuses; ACT's parent corporation, IEC; and ACT's Title IV third-party servicer, Global Financial Aid Services. We also interviewed U.S. Department of Education officials representing Federal Student Aid's Case Management Office, Direct Loan Office, and the Loan Origination Center. We reviewed ACT's written policies and procedures for managing its Title IV programs. We also reviewed ACT's compliance audits for the periods ending October 31, 1998, 1999, and 2000, and its financial statement audits for the periods ending October 31, 1999 and 2000. In addition, we reviewed the compliance attestation audits of ACT's third-party servicer, Global Financial Aid Services, for the periods ending December 31, 1998, 1999, and 2000.

We performed a student eligibility file review in which we reviewed the files of a randomly selected sample of 93 students (from a universe of 3,127) who were enrolled at ACT schools between July 1, 1999, and June 30, 2001, and received Title IV funds per ACT's CLASS accounting system or the Department's National Student Loan Data System (NSLDS). Of these 93 selected students, the school could not locate 4 of the files. Our review of the student ledgers and NSLDS indicated that 3 of these 4 students did not receive student financial aid, nor did 15 of the remaining 89 student files. As a result, we examined 74 files of students who received Title IV funds from ACT during the audit period.

We accomplished the objectives pertaining to the 90/10 Rule by reviewing the 90/10 calculations for FY's 1999, 2000, and 2001. We recalculated the Title IV revenue for these years using ACT's CLASS system posting date data and adjusting for credit balances and cash paid to students. We calculated non-Title IV revenue using the CLASS accounting system posting date data. Due to the incompleteness of the CLASS system (student accounts not posted timely or not at all), we also calculated the 90/10 revenue percentages using the Department's GAPS data.

We accomplished the cash management objective by reviewing the Title IV drawdowns for the Direct Loan, Pell, and FSEOG programs for FY's 1999, 2000, and 2001 and compared these amounts to the amounts posted in ACT's CLASS system. We also traced Direct Loans received by ACT from draw down to posting by reviewing ACT's bank statements, GAPS activity reports, and student ledgers for a judgment sample of the last three months of FY's 1998, 1999, and 2000. Cash management objectives were also reviewed as part of the student eligibility file review and the Direct Loan reconciliation review.

We accomplished the Direct Loan reconciliation objective by reviewing the Direct Loan Student Account Statements (DLSAS) and DLSAS Reconciliation Summary Reports for a judgment sample of the last three months of the 1998-1999 and 1999-2000 Direct Loan awards, and a judgment sample of the last six months for the 2000-2001 Direct Loan award.

To meet the audit objectives pertaining to refunds, we performed a detailed test of a 10 percent random sample (23 of 230 files) of student withdrawals for ACT's 2000-2001 school year to verify refunds and return of Title IV funds. We also reviewed the accuracy and timeliness of refunds as part of our student eligibility file review. We also reviewed the files of the 28 students who withdrew (of the 74 student files showing that the students received Title IV financial assistance).

We reviewed accreditation reports, program participation agreements, State licenses, personnel employment contracts, employee compensation plans, employee payroll ledgers, Wonderlic Ability-to-Benefit score reports, and externship contracts. We reviewed a random sample of 26 students who completed an externship during FY 2001 and analyzed the files to determine whether ACT complied with its externship policies and procedures. We also determined whether ACT complied with the requirements of the Accrediting Council for Continuing Education and Training and State Licensing Boards for the externship program.

To achieve the audit objectives, we relied in part on computer-processed data contained in ACT's CLASS accounting system and the Department's Grant Administration Payment System (GAPS) and NSLDS. The CLASS accounting system contained two date fields to indicate the date that students received Title IV and non-Title IV funds. We determined that the "transaction date" data found in the CLASS system was not verifiable. Since the “posting date” data was automatically generated by the computer system and contained the date that disbursements were actually posted to student accounts, we relied upon the "posting date" data in CLASS for our analyses. We performed limited testing of the CLASS data to assure ourselves that the data were reliable for the purposes of the audit objectives. While conducting the student file review, we compared source information found within the student files to the information recorded in CLASS and NSLDS. While evaluating ACT’s cash management procedures and 90/10 calculations, we examined the dates and amounts of Title IV funds received per GAPS to the dates the funds were posted to student accounts per CLASS. We also performed limited testing of data while recalculating the 90/10 revenue percentages by comparing the information used to calculate the 90/10 percentages to the information in the Department’s GAPS and source documentation to support the calculation that was provided by ACT. Based on the results of our tests we concluded that, except for the transaction date data, the CLASS accounting system data were sufficiently reliable to meet our audit objectives.

Audit work was performed during the period July 2001 through September 2002. We held an exit conference with school officials on December 16, 2002.

The audit was conducted in accordance with generally accepted government auditing standards appropriate to the scope of review described above.

STATEMENT ON MANAGEMENT CONTROLS

As part of the audit, we assessed the system of management controls, policies, procedures, and practices applicable to ACT’s administration of the Title IV programs. Our assessment was performed to determine the level of control risk for determining the nature, extent, and timing of substantive tests to accomplish the audit objectives. For the purposes of this report, we assessed and classified significant controls into the following categories: Institutional eligibility (90/10 revenue percentage, accreditation, and licensing); cash management; student eligibility, Direct Loan reconciliation; and refunds/returns of Title IV funds.

Due to inherent limitations, an evaluation made for the limited purposes described above would not necessarily disclose all material weaknesses in the management controls. We identified no deficiencies with the externship program, or accreditation and licensing. However, our overall assessment disclosed management control weaknesses in each of the other control areas mentioned above. These weaknesses are discussed in the AUDIT RESULTS section of this report.

OIG 90/10 CALCULATION FOR FY 1999
(November 1, 1998, through October 31, 1999)

	OIG FIGURES (GAPS Data)	OIG FIGURES (Post Date Data)	ACT FIGURES 5/ (Transaction Date Data)
Title IV Receipts			
FSEOG 1/	$31,748.00	$10,065.00	
FSEOG Refunds per CLASS Post Date	(120.00)	(120.00)	
Total FSEOG	$31,628.00	$9,945.00	$11,370.00
PELL 1/	$1,563,993.00	$1,579,149.00	
PELL Refunds per CLASS Post Date	(47,348.00)	(47,348.00)	
PELL Credit Balance Adjustments 2/	(2,202.00)	(2,202.00)	
Total PELL	$1,514,443.00	$1,529,599.00	$1,517,063.00
DIRECT LOAN 1/	$4,674,687.00	$4,631,259.01	
Direct Loan Refunds per Post Date	(138,192.50)	(138,192.50)	
Direct Loan Credit Balance Adj. 2/	(2,904.00)	(2,904.00)	
TOTAL DIRECT LOAN	$4,533,590.50	$4,490,162.51	$4,298,150.00
Title IV Cash Adjustments	($4,502.00)	($4,502.00)	
TOTAL Title IV Receipts	**$6,075,159.50**	**$6,025,204.51**	**$5,826,583.00**
Non-Title IV Receipts 4/			
Sale of Retail Installment Contracts	$ 112,670.06	$ 112,670.06	$ 158,744.06
Rehab	11,045.00	11,045.00	11,045.00
Cash	145,006.16	145,006.16	103,239.00
Cash Credit Balance Adjustments 3/	(1,159.00)	(1,159.00)	
Non-Title IV Cash Adjustments	(4,000.78)	(4,000.78)	
Sallie Mae Recourse Loans	538,661.90	538,661.90	785,346.00
Sallie Mae Escrow Adjustment	(41,259.00)	(41,259.00)	(41,259.00)
Sallie Mae Credit Balance Adj. 2/	($211,521.00)	($211,521.00)	
TOTAL Non-Title IV Receipts	**$549,443.34**	**$549,443.34**	**$1,017,115.06**
90/10 Percentage Calculation 6/	**91.7**	**91.6**	**85.1**

NOTES:
1/ GAPS data is net of funds returned by ACT.
2/ The 90/10 calculations can only include funds used to pay for tuition, fees, and other institutional charges. Credit balances were subtracted from the Title IV and non-Title IV figures used for the calculation.
3/ Credit balances paid to students for which ACT did not adjust in its 90/10 calculation.
4/ Data obtained from ACT's CLASS system (posting date data).
5/ Based on the information provided for the financial statement audit.
6/ ACT originally computed 86.2 percent; however, in its written response to the draft audit report, ACT amended non-Title IV revenue figures for Sale of Retail Installment Contracts and the Sallie Mae Escrow Adjustment.

ATTACHMENT B – WRITTEN RESPONSE TO THE DRAFT REPORT

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June 21, 2003

Via Federal Express

Mr. J. Wayne Bynum
Regional Inspector General for Audit
U.S. Department of Education
Office of Inspector General
61 Forsyth Street 18T71
Atlanta, Georgia 30303

Re: Advanced Career Training
ACN: ED-OIG/A04-B0019

Dear Mr. Bynum:

On behalf of Advanced Career Training Institute ("ACT" or the "School"), we hereby respond to the Office of Inspector General's ("OIG") Draft Audit Report dated April 18, 2003 ("Draft Report"), concerning ACT's compliance with the eligibility and administrative requirements applicable to the federal student financial assistance programs under Title IV of the Higher Education Act of 1965, as amended ("Title IV Programs") ("HEA"), Audit Control No. ED-OIG/A04-B0019. This response is timely filed, in accordance with the extension agreed to by your office. Thank you for your courtesy in that regard.

We submit that Finding No. 1 of the Draft Report alleging ACT's failure to meet the requirements of the "90/10 Rule" for fiscal year 1999 (November 1-October 31) is based on an incomplete and faulty analysis of the data underlying the School's 90/10 calculation for that year. Therefore, we believe, as set forth in detail in the attached response, that ACT did satisfy the 90/10 Rule for fiscal year 1999, and thus request that Finding No. 1 be removed when you issue the Final Audit Report.

With respect to the remaining findings, we have provided additional information and responded to each of the recommendations in the Draft Audit Report.

Attached is ACT's response to each of the six findings in the Draft Audit Report, together with supporting exhibits. Please note that Exhibit 3-B, an entire student file, is being submitted in a separate folder, which is enclosed.

ATTACHMENT B – WRITTEN RESPONSE TO THE DRAFT REPORT

If we can provide anything further with respect to any of the findings or the attached response, please do not hesitate to contact us.

Sincerely,

Jonathon C. Glass

Enclosures

cc (w/encl.): Ralph Acaba

ADVANCED CAREER TRAINING INSTITUTE

Response to OIG Draft Audit Report

Finding No. 1: ACT Failed to Meet the 90/10 Rule in FY99

The Draft Report asserts that the School violated the 90/10 Rule for its fiscal year ended October 31, 1999 based on the OIG's adjustment of several factors in the School's calculation, leading the OIG to revise the calculation previously completed by ACT's independent Certified Public Accountant to find that the School received 93.1% of its revenue from the Title IV Programs. The Draft Report therefore concludes that the School was ineligible in the following fiscal year and recommends that the Chief Operating Officer for Federal Student Aid require ACT to return all Title IV funds, approximately $7.4 million, received in fiscal year 2000. The Draft Report is fundamentally flawed in failing to apply cash-basis accounting and in its treatment of third-party loans received by certain students of the School.

LEGAL STANDARDS

The Draft Report relied on the July 1, 1998 volume of the Code of Federal Regulations ("CFR") in effect during the School's 1999 fiscal year to assess ACT's compliance. We have included the relevant sections for ease of review, while updating the language to refer to a 90 percent (rather than 85 percent) threshold, consistent with the HEA Amendments of 1998 (Public Law No. 105-244, enacted October 7, 1998).

Section 102(b) of the HEA provided that a proprietary institution of higher education is one that "has at least 10 percent of the school's revenues from sources that are not derived from funds provided under [the Title IV Programs] as determined in accordance with regulations prescribed by the Secretary." (20 USC § 1002(b)(1)(F)).

Under the Department's regulation at 34 CFR § 600.5(a)(8), a proprietary institution loses its eligibility if it has more than "90 percent of its revenues derived from title IV, HEA program funds, as determined under paragraph (d) of this section." Paragraph (d) set out the formula as follows:

> (1) An institution satisfies the requirement contained in paragraph (a)(8) of this section by examining its revenues under the following formula:
>
> Title IV, HEA program funds the institution used to satisfy tuition, fees, and other institutional charges to students [Numerator].
>
> ---
>
> The sum of revenues generated by the institution from: Tuition, fees, and other institutional charges for students enrolled in eligible programs as

> defined in 34 CFR 668.8; and activities conducted by the institution, to the extent not included in tuition, fees, and other institutional charges, that are necessary for the education or training of its students who are enrolled in those eligible programs [Denominator].

Section 600.5(d)(2) further directs as follows:

> (2) Under the fraction contained in paragraph (d)(1) of this section—
>
> (i) Except as provided in paragraph (h) of this section, the title IV, HEA program funds included in the numerator and the revenue included in the denominator <u>are the amount of title IV, HEA program funds and revenues received by the institution during the institution's last complete fiscal year</u>.

§ 600.5(d)(2) (emphasis added).

ED has also required that an institution's 90/10 calculation be performed using cash-basis accounting. When the 90/10 Rule was promulgated in 1994 (under the "85/15" formula), the Secretary stated in the Federal Register as follows:

> Second, since the institution must report and account for title IV, HEA program funds on a cash basis, the institution must also account for revenue in the denominator on a cash basis. <u>Under a cash basis accounting, the institution reports revenues on the date that the revenues are actually received.</u>

59 Fed. Reg. 22324, 22328 (April 29, 1994) (emphasis added).

Moreover, in proposing to revise the regulation in 1999 to expressly refer to cash basis accounting, the Secretary made clear that he was only making explicit what had been required under this rule from its inception, and went on to explain the essential feature of cash-basis accounting as follows:

> In these proposed regulations, the Secretary makes explicit in § 600.5(d)(2) that an institution must use the cash basis of accounting in reporting Title IV, HEA program funds in the numerator and revenues generated in the denominator of the fraction in § 600.5(d)(1). ...
>
> <u>Under the cash basis of accounting, revenue is recognized by an entity when that entity receives cash</u>, *i.e.*, when there is an inflow of cash to the entity.

64 Fed. Reg. 38272, 38276 (July 15, 1999) (emphasis added).

FACTUAL BACKGROUND

In reviewing this section, we suggest that you consult Exhibit 1-A, which provides a point-by-point comparison of the calculation of the School's 90/10 ratio for fiscal year 1999 as performed by the OIG in connection with the Draft Report and as prepared by the School in connection with this response, showing that the School received 85.1% of its revenues from Title IV Program funds in fiscal year 1999.

1. ACT's independent auditor attested to the School's compliance with the 90/10 Rule in fiscal 1999, including the treatment of third party recourse loans in that calculation. The auditor analyzed the rule and all Departmental guidance available and concluded that the School correctly calculated that it received less than 90% of its applicable revenues from the Title IV Programs. (Copy of the 90/10 Note at Exhibit 1-B).

2. On July 1, 1999, the parent corporation of ACT (International Education Corporation or "IEC") entered into an agreement with an affiliate of Sallie Mae ("Sallie Mae") and Mid-City National Bank ("Sallie Mae Agreement" or "Agreement") under which Sallie Mae agreed to make privately funded loans to students seeking such assistance to attend ACT and who would otherwise not qualify for such loans due to their credit histories or other factors. (Copy of Agreement at Exhibit 1-C). In disbursing loans to these students, Sallie Mae generally issued a wire transmittal document that identified the exact loan amount for each affected student and the exact date the loan funds were received for that student (such as the transmittal documents at Exhibit 1-D).

3. Under section 2.2 of the Agreement, IEC agreed to establish and maintain an escrow account to be equal to 30% of the original principal balance of each loan made by Sallie Mae to ACT students ("Escrow Account"). IEC had the option of funding the Escrow Account through its own payments or agreeing that Sallie Mae could withhold funds for that purpose from new loan disbursements. IEC further agreed to credit the student borrower "with 100% of the Loan amount for payment of tuition and fees or other costs of education" reflecting that these were loans from Sallie Mae to the students for the benefit of the students. Under section 3.1 of the Agreement, in the event that the defaults exceeded the amount then available in the Escrow Account, ACT also agreed to provide additional sums to repurchase any such defaulted loans. Sallie Mae, for its own convenience, actually established multiple accounts to receive and hold escrow funds, but we refer to those accounts here as the Escrow Account.

4. The terms of the Escrow Account were intended to assure funding to pay any defaults by students on Sallie Mae loans. The parties agreed to set the escrow amount at 30% of the total loan principal to satisfy Sallie Mae, which at that time did not have experience in working with IEC or ACT, that they would be able to pay the costs of defaults over the life of the contract. The percentage of coverage in the Escrow Account has varied over the years, and has fallen below 30% from time to time, but IEC or ACT has always made payments to bring the coverage back to 30%, to Sallie Mae's satisfaction. The terms of the Escrow Account never had any effect on Sallie Mae's willingness to make loans to ACT students. Sallie Mae has never declared IEC or ACT in breach of the Agreement with respect to the Escrow Account (or any other term of the Agreement). Sallie Mae has never declined to make loans due to the temporary fluctuations in the coverage percentage in the Escrow Account or any other reason.

5. ACT was not obligated to repurchase any defaulted loans under the terms of the Agreement in fiscal year 1999, since the first loans were made late in fiscal year 1999 and no loans had entered default by October 31, 1999. Throughout fiscal year 1999, ACT and Sallie Mae never needed to draw on the Escrow Account to pay any defaults.

Sallie Mae Loan Funds Adjustment

6. During fiscal year 1999, the School utilized the CLASS software system for accounting for student aid funding, including Title IV funding, and maintaining records regarding student account activity (and the School has continued to use the CLASS system up to the present time). The CLASS system provides a number of data fields to track information related to student accounts, including a "transaction date" and a "posting date."

7. Under the CLASS system, for Sallie Mae loans, the transaction date was entered on a student account only after the School had received the funds with respect to that student. In most cases, such funds were received into the School bank account managed through the IEC corporate office so that, upon receipt, the corporate office personnel would notify the School through a transmittal document that the funds had been received and instruct the School to credit the student's account using the transmittal date as the transaction date.

8. With regard to the School's receipt of loan funds from Sallie Mae, the transaction date was supported by receipts for wired funds, which were dated on or before the transaction date for the affected students. Copies of such wiring records (including the receipts for the loans issued to all 26 students discussed at Points 26-27 below) are at Exhibit 1-D.

9. The precise timing of the School's receipt of loan funds from Sallie Mae is further supported by the School bank statements, which confirm the receipt of the wired funds in October 1999. Copies of the bank statements for the month of October 1999 are also at Exhibit 1-D.

10. With regard to Sallie Mae loans, the transaction date was only entered into the CLASS system after the IEC corporate office or School personnel had confirmed that the applicable funds had been received into the School's bank account and were available, without restriction, to pay the obligations of the student borrowers.

11. Under the CLASS system, in fiscal year 1999 and currently, the posting date is the date that a transaction on a student account is manually keyed into the system. The posting date is automatically generated by the computer system for the principal purpose of documenting data entry so that, at a later date, in the rare event when it might be necessary, the School can determine when and by whom the transaction was entered and any special circumstances regarding the transaction.

12. School personnel have never had any reason to use the posting date for day-to-day financial aid management or accounting purposes and still do not run data reports based on the posting date. The posting date is invisible to the School for financial aid management purposes. School financial aid staff could not and still cannot access data regarding the posting date without the outside assistance of specialized technical staff. Because the OIG ran certain data reports using the posting system, the School has also used the posting date to prepare certain

- 4 -

exhibits to this response, but otherwise the School staff do not use the posting date for any financial aid or accounting purposes.

13. The School did not and does not treat the posting date as a disbursement date. All funds are considered credited to the student's account as of the transaction date entered for those funds. For instance, if student comes to the business office to confirm that certain funds have been entered on their account, the School examines the student ledger and uses the transaction date on the ledger card to confirm the date and amount of the payment.

14. A representative of Campus Management, Inc., which developed the CLASS system, has confirmed that the posting date is not intended to capture the date that student aid funds are credited to the student's account, and is not intended for financial aid management purposes, including the calculation of an institution's 90/10 ratio. Campus Management personnel have confirmed that the "Cash Receipt Report" is the standard report used to measure 90/10 compliance by other institutions that use the CLASS system, and the School used such Cash Receipt Report to calculate its 90/10 ratio in fiscal year 1999 and subsequent years.

15. The Draft Report uses the posting date to determine when funds, including Sallie Mae loan funds, were received for purposes of the 90/10 Rule. "To determine revenue for the 90/10 calculation, we used the CLASS system posting date data because it represented the date that funds were actually disbursed to students." (Draft Report at page 4).

16. Based on this methodology, the OIG only counted Sallie Mae loans in the denominator of the School's 90/10 ratio if such loans had a posting date on or before October 31, 1999, resulting in the inclusion of a total of $538,662 in Sallie Mae loans according to the Draft Report. In following this method, the Draft Report excludes $246,684 in Sallie Mae loan funds for 26 students whose accounts had transactions dates prior to October 31, 1999, but posting dates on or after November 1, 1999. These students and loan funds are identified on the spreadsheet at the first page of Exhibit 1-D. (We have not included the student ledger cards since the OIG already has such ledger cards as part of the CLASS system data provided by the School.)

17. In the case of all 26 students, the School had received the $246,684 from Sallie Mae on or before the transaction date, so that all $246,684 was received in fiscal year 1999 (as shown in the wiring records and bank statements at Exhibit 1-D).

18. The total Sallie Mae loan funds received by the School in fiscal year 1999 was correctly reported by the School and its auditor in Note 3 of the 1999 audited financial statements as $785,346 ($538,662 plus $246,684). (Copy of Note 3 at Exhibit 1-E).

19. The spreadsheet at the first page of Exhibit 1-D demonstrates that the Sallie Mae loans for 21 of the 26 students had a posting date of November 1, 1999. The total value of these loans with the November 1, 1999 posting date was $218,895.

Sallie Mae Escrow Adjustment

20. The Draft Report (at page 4) adjusts the Sallie Mae loans included in the denominator of the 90/10 ratio by reducing the total loan principal by the 30% that would be paid

into the Escrow Account, as referenced in section 2.2 of the Agreement. Thus, the OIG input its own figure of $161,599 (representing 30% of the loan amount of $538,662, as recognized by the OIG), even though actual cash transactions in the Escrow Account were significantly less.

21. As of October 31, 1999, the sum of $41,259 had been deposited in the Escrow Account by the School or Sallie Mae. This figure is slightly higher than the figure cited by the OIG in the Draft Report due to the discovery of one additional payment to the Escrow Account.

22. Subsequently, in fiscal year 2000, the School made payments to bring the Escrow Account up to the customary 30% coverage. All funds paid into the Escrow Account in fiscal year 2000 were deducted from the value of the Sallie Mae loan funds in the calculation of the School's 90/10 ratio in fiscal year 2000, consistent with the cash-basis accounting under the 90/10 Rule.

23. ACT has calculated the value of the Sallie Mae loans for purposes of its 90/10 calculation on a cash basis consistently for fiscal 1999 and subsequent years, following the same method in each year to determine the value of those loans as revenue in the denominator of the 90/10 ratio. ACT has counted the loan funds actually received by the School in the relevant fiscal year, as reduced by the funds (i) actually paid by ACT to the Sallie Mae Escrow Account, (ii) actually withheld by Sallie Mae and placed into such Escrow Account, (iii) actually paid by the School for Sallie Mae loan refunds, and (iv) actually paid by the School to eliminate Sallie Mae loan credit balances, in each case in the relevant fiscal year. As a result, if payments to the Escrow Account (or any of the other referenced payments) were actually made in the last month of a given fiscal year such payments were deducted in the fiscal year ending that month. Similarly, any such payments made in the first month of a given fiscal were deducted from the 90/10 calculation for the fiscal year beginning that month.

Sallie Mae Credit Balance Adjustment

24. The Draft Report (at page 5 and Exhibit A) reduces the value of the Sallie Mae loan funds based on credit balances in the amount of $148,065. The OIG actually identified a total of $211,521 in credit balances on the accounts of the affected students, and the OIG reduced that figure by 30% since the OIG already had reduced the School's Sallie Mae loan principal balance by 30% based on the OIG's interpretation of the requirements of the Escrow Account (as discussed at Point 20 above). Thus, the $148,065 is an adjusted figure (70 percent of $211,521). A listing of the credit balances for the affected students is at Exhibit 1-F.

25. The OIG's adjustment for credit balances is based entirely on credit balances recorded on the students' accounts, without regard to when those credit balances were paid.

Sale of Institutional Retail Installment Contracts

26. The School concluded the sale of institutional retail installment contracts ("RIC," also referenced as student retail installment agreements in certain exhibits) on October 29, 1999, that resulted in the receipt of an additional $90,295 in non-Title IV funds in fiscal year 1999. This sale transaction was mistakenly overlooked and the sale proceeds were not included in the 90/10 calculation as originally performed by the School and its auditor. The School discovered the sale documents in preparing this response and presents them to the OIG for the first time in

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connection with this response. This $90,295 was the payment received from an independent third party, as demonstrated by the wire transfer records and purchase agreement at Exhibit 1-G.

27. The wire transfer records are both dated October 29, 1999. The first record refers to a transfer of $90,295 (for ACT) and a second non-ACT transfer of $90,000. The record entitled "Incoming Wire Transfer Advice," states at the top that: "This funds transfer has been received on behalf of your customer on 1999-10-29," and goes on to name Advanced Career Training as the beneficiary. The $90,295 is further confirmed in the purchase agreement, backed up by the 15-page schedule to the purchase agreement, which identifies the student RICs that were transferred for cash. The purchase agreement was non-recourse.

DISCUSSION

The Draft Report makes certain fundamental errors in its application of cash-basis accounting and other aspects of the recalculation of the School's 90/10 ratio that reduce the gross value of the Sallie Mae loans received and inflate certain factors that lead to even further reductions in the value of such loans for purposes of the School's 90/10 ratio. In addition, the School has identified documentation to substantiate the sale of student RICs in fiscal 1999 that generated an additional $90,295 in non-Title IV revenue received in that year.

The OIG's and the School's calculations are displayed on a comparative basis at Exhibit 1-A. These charts are prepared in the same form as the OIG's chart labeled as Exhibit A in the Draft Report, using the figures from the column labeled "OIG FIGURES (Post Date Data)" since the OIG used the posting date to determine the transactions included in this calculation. (See Point 15 above).

Non-Title IV Revenue in Denominator

This portion of the response focuses exclusively on the treatment of the Sallie Mae loans as a source of non-Title IV revenue to be counted in the denominator of the School's 90/10 ratio as recalculated by the OIG. For purposes of this response, the School does not dispute the treatment of other items in the OIG calculation of non-Title IV revenue.[1]

1. Sallie Mae Loan Revenue

The Draft Report uses the figure of $538,662 as the total loan principal received by the School from Sallie Mae loans in fiscal year 1999. This figure is derived from the funds that were

[1] The Draft Report confirms that the Sallie Mae recourse loans qualify to be counted as non-Title IV revenue in the denominator of the 90/10 calculation, although we disagree with the OIG as to the adjustments to arrive at the correct valuation. Accordingly, we do not discuss the fundamental nature or characteristics of the Sallie Mae loans in detail, but focus our discussion solely on the challenged adjustments. We reserve our right to reexamine the nature and characteristics of the Sallie Mae loans and submit new evidence on that subject if that becomes necessary.

indicated with a posting date in fiscal 1999, since the OIG used the posting date under the CLASS system to determine if the funds were received on or before October 31, 1999. The OIG rejected the School's figure of $785,346 in Sallie Mae loans, which was derived by identifying loans according to the transaction date in the CLASS system, even though the transaction date represented loan funds actually received by the School from Sallie Mae on or before the transaction date indicated on the student's account record. The OIG's method results in a significant reduction in the Sallie Mae loan revenue as calculated by the School and its auditor, since there were Sallie Mae loans to 26 students, with a total value of $246,480, that had transaction dates in fiscal year 1999 but posting dates on or after November 1, 1999 that were excluded from the OIG's recalculation. These 26 loans, with the related wiring and bank records, are identified at Exhibit 1-D.

The OIG's use of the figure derived from the posting date rather than the transaction date is wrong as a matter of fact and law. The Draft Report (at page 4) states that "the 'transaction date' field contained the date that the transaction should have occurred per ACT/IEC officials. ACT/IEC staff entered the transaction dates into the CLASS system." Thus, the Draft Report would suggest that the transaction date is nothing but a prediction of the date that a transaction "should" occur. This is a fundamental misunderstanding, which ignores that the School never determined and entered the transaction date for Sallie Mae loans into the CLASS system until such funds had been received into the School's bank account. (See Point 10 above). Further, the School treated, and continues to treat, the transaction date as the date that funds are credited to the student's account. The posting date has no purpose in the School's normal financial aid or accounting operations, and the OIG is the only party that has ever used the posting date to generate data reports for financial aid purposes. (See Point 12 above). Campus Management, Inc., the creator of the CLASS system, also has advised the School that the CLASS software is not designed for any institution to use the posting date for financial aid management or to use that date as the equivalent of a disbursement date. (See Point 14 above).

The issue of how to calculate the Sallie Mae loan revenue in the School's ratio must be analyzed under the precise terms of the 90/10 Rule, and specifically the requirement to focus on the funds "received" by the institution in the applicable year. The Rule in effect in fiscal 1999 stated:

> (2) Under the fraction contained in paragraph (d)(1) of this section
>
> > (i) Except as provided in paragraph (h) of this section, the title IV, HEA program funds included in the numerator and the revenue included in the denominator are the amount of title IV, HEA program funds and revenues <u>received</u> by the institution during the institution's last complete fiscal year.

34 C.F.R. § 600.5(d)(2)(i) (emphasis added). By its terms, the regulation requires no more than that the funds be "received" by the institution, which is satisfied when the funds are deposited into the institution's bank account.

The Draft Report would suggest an additional requirement that the funds be received <u>and</u> posted to the student's account to be included in the 90/10 calculation, but no such requirement exists in the regulation. Moreover, the additional requirement as proposed in the Draft Report would be flatly inconsistent with cash-basis accounting. As the Secretary has explained, cash-basis accounting measures when the funds are received; no more and no less.

> Second, since the institution must report and account for title IV, HEA program funds on a cash basis, the institution must also account for revenue in the denominator on a cash basis. Under a cash basis accounting, the institution reports revenues on the date that the revenues are actually received.

59 Fed. Reg. 22324, 22328 (April 29, 1994) (emphasis added). In a subsequent rulemaking, the Secretary reemphasized the meaning of cash basis accounting: "Under the cash basis of accounting, revenue is recognized by an entity when that entity receives cash, *i.e.*, when there is an inflow of cash to the entity." 64 Fed. Reg. 38272, 38276 (July 15, 1999) (emphasis added).

The only section of the 90/10 Rule that even mentions whether funds were "disbursed" or "delivered" to the student is paragraph (d)(2)(v), which is written with specific reference to the "presumption" that Title IV funds (in the numerator) are presumed to be used to pay tuition, fees and institutional charges. This paragraph does not state or even imply, as the Draft Report would suggest, that funds are not "received" under cash basis accounting, to be included in the denominator, until they are disbursed to the student, and there is no basis for the OIG to invoke a disbursement requirement for any other purpose in the 90/10 Rule.

The Draft Report would ignore the meaning of the transaction date as intended under the CLASS system and as implemented by ACT with respect to the Sallie Mae loan funds. The School actually treated (and continues to treat) the transaction date as the date that funds were credited to its students' accounts as a payment of the student's obligations, as is correct under the CLASS system. (See Points 13-14 above). Under the Sallie Mae Loan Agreement, it is clear that Sallie Mae actually disbursed funds to the students (as identified by name and exact dollar amount on the wire transmittals) when it wired funds on behalf of those students to the School's bank account. (See Point 2 above). The School then entered a transaction date on the student's account to reflect that the funds for that student had been received and credited as a payment on the student's account on or before such transaction date. Accordingly, the full amount of $246,684 for the loans with transaction dates prior to October 31, 1999 must be counted in the denominator of the School's 90/10 ratio for fiscal year 1999.

In addition, it is notable that 21 of the 26 loans in this group have a posting date of November 1, 1999. For these 21 loans, in the amount of $218,895, the School made the manual accounting entry that generated the posting date on November 1st, the very first business day following the close of fiscal year 1999. For the Draft Report to deny that these loans belong in fiscal year 1999 is to suggest that this issue should be decided by the mechanical question of when certain entries were made in the School's CLASS system, rather than when the funds were actually received by the School (as documented by the wire and bank records) and credited by the School to the student's account to pay the student's charges (as reflected by the transaction date on the ledger card). The Draft Report is ignoring the actual meaning of the transaction date in the School's records to focus on the sheer happenstance of whether a School employee stayed late on Friday, October 29, 1999, to make certain accounting entries, or waited until Monday, November 1, 1999, to make those entries. Thus, the OIG is not only mischaracterizing the meaning of the transaction date and posting date within the School's CLASS system, but also is placing form entirely over substance in analyzing this issue.

In sum, as the Secretary has explained in unequivocal terms, cash-basis accounting focuses exclusively on when cash is received or paid. It is plain that funds that have been deposited in an institution's bank account for the use of the institution have been received by that institution. The 90/10 Rule requires only that funds be received to be included in the ratio, and the additional $246,480 in Sallie Mae loan funds identified at Exhibit 1-D were received in October 1999. These funds must be counted for a total of $785,346 in Sallie Mae loan funds in the denominator of the School's 90/10 calculation in fiscal year 1999.

2. Sallie Mae Escrow Adjustment

The Draft Report proposes to adjust the total Sallie Mae loan principal for escrow payments referenced under the Sallie Mae Loan Agreement, as if the OIG were in the position to enforce the terms of such Agreement. The OIG does so by reducing the total loan principal by 30% to reflect the amount to be paid into the Escrow Account, pursuant to Section 2.2 of the Agreement. Thus, the 90/10 calculation in the Draft Report reduces the Sallie Mae loan principal by $161,599 (30 percent of the $538,662 in Sallie Mae loan revenue accepted by the OIG). The $161,599 is a derived number that has no relation to the cash transactions in the Escrow Account as of October 31, 1999 or even as of a future date.

Under cash-basis accounting, the only proper basis to adjust for payments to the Escrow Account is to reflect actual payments to the Escrow Account. As of October 31, 1999, the School had paid a total of $41,259 into the Escrow Account (see Point 21 above), and that is the entire amount that properly can be subtracted from the Sallie Mae loan funds on the basis of an escrow adjustment.

Additional funds that the School paid into the Escrow Account in the subsequent month, November 1999, were deducted in the School's 90/10 calculation for fiscal year 2000. (See Point 22 above). Thus, the School has accounted for every penny actually paid into the Escrow Account on a consistent cash-basis, with all funds counted in the year in which they were paid.

The Draft Report's position on this issue would transform cash-basis accounting into a hybrid of cash-basis and accrual accounting. The OIG would go beyond tracking the date that cash was actually paid or received, and consider other factors relating to the rights and duties of an institution under a contract with a third party (the Sallie Mae Loan Agreement) to evaluate when funds may or not be considered "available" under such contract. (See Note 4 of Exhibit A). The Draft Report (at page 5) goes so far as to say that the OIG construed the Sallie Mae Loan Agreement to determine that ACT was not "entitled to receive" the entire cash amount of the loans, while ignoring that ACT had in fact "received" that entire amount in the form of deposits in its bank account in fiscal year 1999 and that each student's account had been properly credited by the School before the close of that fiscal year, as reflected by the transaction date on the student's account. The consideration of such contractual rights or obligations is not relevant to cash-basis accounting. Indeed, to introduce such factors is to introduce certain principles of accrual accounting into the cash-basis system. Moreover, as set forth at Point 4 above, Sallie

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Mae has never challenged the School's handling of the Escrow Account and has never withheld loans based on any concern with the status of the Escrow Account. Thus, the OIG's method is wrong and its concern is simply misplaced. The OIG is attempting to raise an issue under the Sallie Mae Loan Agreement that had no effect on the availability of funds provided pursuant to that Agreement in fiscal year 1999. The only funds that can properly be deducted in fiscal year 1999 based on the Escrow Account are funds paid into the Escrow Account in fiscal year 1999, or $41,259.

3. **Sallie Mae Credit Balance Adjustment**

The OIG also has significantly reduced the value of the Sallie Mae loans received by the School by subtracting for credit balances on the students' accounts. The Draft Report (at page 5 and Exhibit A) reduces the value of the Sallie Mae loan principal based on credit balances in the amount of $148,065.[2] That figure represents a 30% reduction of the $211,521 in credit balances on the student accounts, as shown at Exhibit 1-F. The OIG made the 30% adjustment since the OIG also reduced the School's Sallie Mae loan principal balance by 30% based on the OIG's interpretation of the requirements of the Escrow Account. (See Point 24 above).

The $148,065 is a derived figure, calculated by the OIG without regard to when the credit balances were actually paid. The OIG's calculation on this point is another effort to inject extraneous factors into the cash-basis accounting required under the 90/10 Rule. The only adjustment that can properly be made for credit balances is an adjustment that reflects when those credit balances were actually paid. With regard to the students listed at Exhibit 1-F, those credit balances were paid in fiscal year 2000 and those payments reduced the value of Sallie Mae loans in the School's 90/10 calculation for fiscal year 2000. (See Point 23 above). The OIG's method would actually force the School to "double count" for credit balances, in fiscal years 1999 and 2000.

In this regard, it is significant that as of fiscal year 1999 the Department had not issued any regulatory guidance specifically addressing the treatment of credit balances in the 90/10 calculation. While the Secretary issued guidance in the Federal Register of October 29, 1999 (64 Fed. Reg. 58608 at 58610) indicating that funds held as credit balances generally are not counted in an institution's 90/10 calculation, that guidance was published on the last business day of the School's fiscal year 1999, in connection with regulatory revisions that did not take effect until July 1, 2000. As a result, the exclusion of credit balances from the 90/10 calculation was not expressly called for until fiscal year 2000, and the School properly tallied its credit balances in fiscal year 1999 according to the cash basis accounting mandated in the 90/10 Rule.

Assuming, solely for the sake of argument, that the OIG maintains its position that an adjustment for credit balances is required, the School has performed an alternative 90/10 calculation (at Exhibit 1-H) based on the OIG's position. In reviewing that alternative

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[2] The Draft Report (at page 5) also refers to adjustments for Title IV credit balances, but no such adjustments are explained or evident on the face of the calculation at Exhibit A. The School reserves its right to reexamine any Title IV credit balance adjustments if the OIG identifies any with specificity.

calculation, note that the OIG's original credit balance figure did not incorporate the Sallie Mae loans to the 26 students (in the amount of $246,684) who were incorrectly excluded from the calculation due to their posting dates. These 26 students had $114,112 in credit balances on their accounts as of October 31, 1999. (See Exhibit 1-T). (We have not included the student ledger cards since the OIG already has such ledger cards as part of the CLASS system data provided by the School.)

These credit balances, plus the $211,521 in credit balances previously identified by the OIG, produce a total value of $325,633 for all Sallie Mae credit balances ($211,521 plus $114,112) as of the end of the fiscal year. Rather than making a 30% percentage reduction in the value of the credit balances as proposed by the OIG, in its revised calculation the School has reduced the total Sallie Mae loan principal by the full amount of the credit balances ($325,633) on all Sallie Mae loans.[3]

Under this calculation, when the School receives the full value of $785,346 of Sallie Mae loans received in fiscal year 1999, and even after reducing that figure by the full value of the credit balances and the Escrow Account, the School derived just 89.2% of its revenue from Title IV sources ($6,025,205/$6,753,294). ACT emphasizes that it does not accept the OIG's treatment of credit balances as correct for fiscal year 1999, and it has submitted this alternative calculation solely to demonstrate that, even under the most conservative treatment of credit balances, the School still satisfied the 90/10 Rule in fiscal year 1999.

4. Sale of Student RICs

The School's calculation includes an additional $90,295 in the denominator for the sale of student RICs that was concluded in October 1999, but was mistakenly overlooked when the School and its auditor performed their original 90/10 calculation. In accordance with the cash-basis accounting procedures for the 90/10 calculation, ACT has counted only the funds received in fiscal year 1999 on the sale of such RICs.

The receipt of $90,295 is demonstrated in the wire transfer records and purchase agreement at Exhibit 1-G. The wire transfer records are both dated October 29, 1999. The second record, entitled "Incoming Wire Transfer Advice," states at the top that: "This funds transfer has been received on behalf of your customer on 1999-10-29," and goes on to name Advanced Career Training as the beneficiary. The $90,295 is further confirmed in the purchase agreement, backed up by the 15-page schedule to the purchase agreement, which identifies the student RICs that were sold in fiscal year 1999, generating revenue received by the School in fiscal year 1999.

[3] However, since the OIG has made certain modifications to cash-basis accounting in the recalculation in the Draft Report, the School reserves the right to revise its credit balance adjustment to be consistent with the modifications proposed by the OIG.

Title IV Revenue in Numerator

For purposes of this response, we have accepted the OIG's figure of $6,025,205 in Title IV revenue in the numerator of the School's 90/10 ratio. However, we note that the School's calculation of its Title IV revenue at the time of the audit was $5,826,583, approximately $200,000 less than the OIG's figure, and we reserve the right to reexamine the OIG's calculation of Title IV revenue and submit new evidence on that point if that becomes necessary.

* * * *

Based on the adjustments discussed above, the School's 90/10 ratio in fiscal year 1999 should be corrected to show Title IV funding represented 85.1% of total revenue ($6,025,205/$7,078,927), as shown at Exhibit 1-A. This calculation follows cash-basis accounting by including the additional $246,480 in Sallie Mae loans, reduced by $41,254 actually paid into the Escrow Account, and also including the $90,295 for the sale of RICs.

In addition, the School satisfies the 90/10 Rule under the alternative calculation that is based on the OIG's position on credit balances, as demonstrated at Exhibit 1-H. This calculation is the same as discussed in the prior paragraph except that the School would exclude the full value of the credit balances from the total Sallie Mae loan revenue.

Accordingly, we ask that Finding No. 1 be eliminated in the Final Report.

Finding No. 2: ACT Breached Its Fiduciary Responsibility Regarding the Use of Title IV Funds

Finding No. 2 states that ACT did not maintain Title IV funds in an interest-bearing account identified as containing federal funds until the funds were disbursed to students, and that ACT did not disburse Title IV funds to students within three business days following the date the institution received the funds.

At the outset, ACT will concede that for the period covered by the OIG audit, which was school fiscal years 1999, 2000 and 2001, it did not consistently disburse Title IV funds to students in accordance with all applicable ED requirements. ACT would like to address that situation for that time period and describe the policies and procedures that have subsequently been implemented to assure compliance with applicable regulations.

First of all, ACT wishes to confirm that during award years 1998-99 and 1999-2000, it did always draw down Title IV funds into an interest-bearing account identified as containing federal funds. A listing of the banks and the account names and numbers is provided as Exhibit 2-A.

During award year 2000-01 to the present, ACT has always maintained Title IV funds in bank accounts identified as containing federal funds. See Exhibit 2-B for a listing of these banks and the account names and numbers. During this period, however, these federal funds accounts were not interest-bearing accounts because ACT determined that the interest that would be earned on the funds in the accounts would be less than the required regulatory minimum of $250 per year. ED regulations at 34 C.F.R. § 668.163(c)(3) provide that an institution does not have to maintain Title IV funds (other than Perkins Loan funds) in an interest-bearing account if the institution will not earn over $250 on those funds during the award year. ACT discussed this regulatory requirement thoroughly with its third-party servicer, Global Financial Aid Services, and determined that the interest that would be earned on its federal funds accounts would be less than $250 annually. This is due to the limited volume of Title IV funds drawn by the school, ACT's practice of transferring the Title IV funds out of those accounts within one day, and the low rate of interest earned on such accounts.

For example, ACT currently draws down approximately $6 million in Title IV funds each year. The interest rate available on such accounts is currently 1.2 percent. Assuming all funds drawn are held in the federal funds accounts for one day, one day's interest on $6 million at 1.2 percent is approximately $200. ACT has been told by the banks where its federal funds accounts are located that the wire transfer fees charged by the banks for such accounts would be several times that amount, approximately $4,000 per year. Therefore, ACT determined it was not cost effective to place these funds in interest-bearing accounts, so long as the anticipated annual interest amount was below the regulatory threshold. If the OIG has any further specific guidance on this point, ACT would appreciate receiving it.

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As indicated, it was ACT's practice during the years covered by the audit to transfer the Title IV funds it received out of the federal funds account and into its operating account approximately one day after their receipt from ED. ACT did this because a predominant number of ACT students use all of the Title IV funds awarded to them to pay institutional charges (i.e., tuition, fees, books and related charges). It was ACT's intent that, immediately upon transfer of the funds to the institutional operating account, it would credit the funds to the students' tuition accounts. Unfortunately, during the period covered by this audit, this did not always happen on a consistent basis, and funds were not consistently credited to students' accounts within three business days, as the OIG determined and verified. ACT concedes that practices like this that were initiated by the prior management of ACT's parent company were sometimes too informal and, therefore, not consistent with applicable federal regulations.

ACT has made several significant changes to institutional policies and operations to address this problem. First, in 2000, ACT engaged the services of Global Financial Aid Services, an experienced third-party servicer, to handle key aspects of ACT's draw down and disbursement of Title IV funds. Global determines each student's eligibility to receive Title IV funds, calculates each student's need and awards their Title IV aid, prepares each Title IV funds request to ED, receives the Title IV funds from ED, and handles all related Title IV cash management functions. Global provides these same services to many dozens of other institutions, and ACT believes that Global is generally regarded as one of the most professional and respected servicers in the country.

In addition, ACT implemented new procedures in 2002, and enhanced them further in 2003, which have dramatically reduced the time lapse between the date Title IV funds are drawn down and the date those funds are credited to students' accounts.

ACT's current policy is that Federal Pell Grant funds and campus-based Title IV funds not be drawn down and transferred to the institution's operating account until those funds have been credited to students' accounts. When Global determines that the student is eligible for the disbursement of funds, it creates a roster indicating the student's name and amount of Pell or campus-based funds scheduled to be disbursed. The roster is transmitted to the institution, and the institution credits the funds to the student's account. Confirmation that the funds have been credited is transmitted to Global, which draws down the funds at that time. See Exhibit 2-C for current procedures and related training materials. Global has implemented this policy for ACT, which eliminates the possibility that the funds would sit in the institution's account for an undue period before being disbursed to students' accounts. Beginning in July 2003, ACT and Global will process Federal Direct Loan funds in the same manner as Pell and campus-based funds.

An analysis of Title IV funds transactions during calendar year 2002 demonstrates that, except for very few instances, Title IV funds were distributed to students' accounts within three business days of their receipt from ED. The following analysis is for a sample of 211 randomly selected students from the population of approximately 2,000 students who received Title IV funds in calendar year 2002. These 211 students had 1,133 transactions (credits of Title IV funds to accounts). Of those 1,133 transactions, 97.5% (1,105 transactions) were credited to the students' accounts in three business days or less, and another 2% (22 transactions) were credited to students' accounts in four to seven days. Only six transactions, representing 0.5% of the total transactions, were credited to students' accounts after more than seven days. Attached as Exhibit

2-D is a spreadsheet documenting the number of days between the date the funds were received and the date they were credited to these students' accounts.

With respect to the specific recommendations made in the Draft Audit Report, ACT requests the OIG's guidance with respect to placing Title IV funds in an interest-bearing account, given the likely amount of interest to be earned, as described above (Recommendation 2.2). Subsequent to the audit, ACT has implemented procedures to ensure that Title IV funds are disbursed to student accounts within three business days following the date the funds are received (Recommendation 2.3). Finally, with respect to Recommendations 2.1 and 2.4, ACT wishes to emphasize that the Draft Audit Report describes past procedures and a problem that went back as far as five years ago. ACT has taken numerous steps to revise its practices, including the retention of a respected third-party servicer, to help administer its Title IV funds appropriately and to help ensure these past practices will not continue. For those reasons, ACT does not believe that it should be placed on reimbursement, or that its Title IV participation should be limited, suspended or terminated, and ACT requests that those recommendations be removed from the Final Audit Report.

Finding No. 3: ACT Improperly Disbursed Title IV Funds to Ineligible Students

Finding No. 3 states that ACT improperly disbursed Title IV funds to 16 students, for four different reasons. ACT will address each of the four groups separately.

A. Disbursements More Than 90 Days After Student's Last Date of Attendance

The Draft Audit Report cites late disbursements for eight students and recommends that a total of $25,081 be returned to ED. These students are examples of the procedural weakness at ACT identified by the OIG in Finding No. 2 above. That is, in virtually all of these cases, the student was enrolled and eligible for these Title IV funds at the time the funds were drawn down from ED, but there was a delay in crediting the funds to the student's account. Several of these students completed their program at ACT and graduated. Following is an explanation of the circumstances surrounding each student.

1.

ACT records indicate $1,294 for an Unsubsidized Federal Direct Stafford Loan was drawn down March 7, 2000 and $2,586 in additional Unsubsidized loan funds was drawn down March 14, 2000. (The remaining amount of the questioned cost for this student is the origination fee on the loan, not received by the school.) The student graduated May 12, 2000, and thus her last day of attendance was May 12, 2000.

This student was eligible for the $3,880 in questioned Title IV funds when they were drawn down, which was well prior to the student's last day of attendance.

A subsequent review of the student's account revealed that the above indicated funds had not been credited to the student's account. The error was rectified December 28, 2000 (posting date) with a transaction date of December 1, 2000, which was admittedly more than 90 days after the student's last date of attendance.

2.

ACT records indicate $1,273.00 for a Subsidized Direct Stafford Loan was drawn down September 21, 2000. Several months later, the student withdrew from school, with a drop determination date of March 13, 2001 and a last date of attendance of February 23, 2001.

Thus, this student was eligible for the $1,273 in questioned Title IV funds when they were drawn down, which was well prior to the student's last date of attendance.

A subsequent review of the student's account revealed that the above indicated funds had not been credited to the student's account. The error was rectified April 30, 2001 (posting date) with a transaction date of April 1, 2001. This was within 90 days of the student's last date of attendance.

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3.

ACT records indicate the following loan funds were drawn down on behalf of this student:

Subsidized/Direct Stafford		Unsubsidized/Direct Stafford	
Date	Amount	Date	Amount
9/3/99	$848	9/3/99	$1,293
12/27/99	$849	12/27/99	$1,294
3/14/00	$849	3/14/00	$1,294

The student began classroom attendance August 2, 1999 and dropped March 17, 2000 with a last day of attendance of March 8, 2000. The student re-entered school August 5, 2000, and graduated August 10, 2000 with a last day of attendance of August 10, 2000.

The student was eligible for the funds drawn down on September 3, 1999 and December 27, 1999 (totaling $4,284), which was well before the student's drop date of March 17, 2000 and LDA of March 8, 2000.

There was a delay in crediting this $4,284 to the student's account, as follows, but these funds were eventually all credited to his account:

Subsidized/Direct Stafford			Unsubsidized/Direct Stafford		
Post Date	Trans Date	Amount	Post Date	Trans Date	Amount
6/12/01	9/10/99	$848	4/20/01	9/3/99	$1,293
6/12/01	12/27/99	$849	4/20/01	12/27/99	$1,294

The additional $2,143 in Stafford loans that was drawn down March 14, 2000 was credited to the student's account as follows:

Subsidized/Direct Stafford			Unsubsidized/Direct Stafford		
Post Date	Trans Date	Amount	Post Date	Trans Date	Amount
6/12/01	3/14/00	$849	4/20/01	3/14/00	$1,294

ACT acknowledges that the student was not eligible for the $2,143 drawn down March 14, 2000. However, it wishes to point out that the student regained eligibility for the funds upon re-entering August 5, 2000, and the student successfully completed the program August 10, 2000.

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4.

ACT records indicate $30 in SEOG funds were drawn down March 20, 2001 and $883 in Pell funds were drawn down April 19, 2001. (Those amounts, plus $10 in institutional contribution for the federal SEOG funds, total $923.) The $30 in SEOG funds were credited to the student's account April 5, 2001 (post date) and a transaction date of March 20, 2001. The Pell funds were credited to the student's account April 27, 2001 (post date) and a transaction date of April 19, 2001.

The student graduated October 30, 2000 with an LDA of October 27, 2000. The institution acknowledges that the $913 in Title IV funds (SEOG federal share of $30 and Pell of $883) were drawn down more than 90 days after the student graduated from her program of study.

5.

It appears the OIG may have misinterpreted this student's file, as it does not appear to be a case of a late disbursement.

ACT records indicate that $30 in SEOG funds (federal capital contribution) were drawn July 6, 2000 and an additional $30 in SEOG funds were drawn July 11, 2000. (Those amounts plus $20 in institutional matching contribution total the $80 in questioned costs.)

ACT records indicate that on July 6, 2000 (transaction date) with a posting date of July 13, 2000, the student's account was incorrectly credited with $120 in SEOG FCC described as "FSEOG 2000-01." On July 13, 2000 (transaction date) with a posting date of July 13, 2000, the school again incorrectly credited the student's account with $120 in SEOG FCC, described as "FSEOG 1999-00."

The above two erroneous entries (award years and amounts) were reversed on October 1, 2000 (transaction date), and the correct entry of $60 in SEOG FCC (1999-2000) was made on October 1, 2000 (transaction date).

With respect to the specific reason for which this student was cited, ACT wishes to point out that the student began classroom attendance June 12, 2000 and dropped July 31, 2000 with a last date of attendance of June 26, 2000. Therefore, the SEOG funds drawn July 6 and 11, 2000 and credited to the student's account on July 6 and 13, 2000 were disbursed before the student's drop date (July 31, 2000) and within 90 days of her last day of attendance (June 26, 2000).

6.

ACT records indicate $1,274 in Subsidized Direct Stafford and $1,940 in Unsubsidized Direct Stafford loans were drawn down September 21, 2000. The funds were drawn in anticipation of first loan disbursements due to the student. The student began classroom attendance July 24, 2000, dropped January 18, 2001 with a last date of attendance of December 29, 2000, re-entered August 20, 2001, and graduated October 19, 2001.

The student was thus eligible for these funds when they were drawn down. A subsequent review of the student's account revealed that the above funds had not been credited to the student's account. The funds were credited to the student's account April 30, 2001 (post date) with a transaction date of April 1, 2001. This was prior to the student's ultimate last date of attendance, her graduation date of October 19, 2001.

7.

ACT records indicate the student began classroom attendance at the Riverdale, Georgia campus of ACT and subsequently transferred to the Atlanta, Georgia main campus. The locations are approximately 20 miles apart. Student account ledgers and attendance records were maintained at both campuses. The student's ledger accounts reflect the following Title IV transactions:

RIVERDALE CAMPUS				
Program	Draw Date	Post Date	Trans Date	Amount
SEOG FCC	11/12/99	11/24/99	11/12/99	$30
Pell	11/12/99	11/24/99	11/12/99	$1,041
Sub	12/13/99	12/18/99	12/13/99	$848
Pell	*	11/2/01	1/1/00	$1,042
Sub	3/7/00	3/9/00	3/7/00	$848
Unsub	2/16/00	1/3/01	12/1/00	$1,293
Unsub	3/7/00	1/3/01	12/1/00	$1,293
Unsub	**	12/12/01	12/11/01	($849)

ATLANTA CAMPUS				
Program	Draw Date	Post Date	Trans Date	Amount
SEOG FCC	5/25/00	6/21/00	6/1/00	$30
Pell	5/25/00	6/21/00	6/1/00	$1,042
Sub	4/24/00	5/5/00	4/24/00	$849
Sub	12/13/99	4/18/01	4/1/01	$848†
Unsub	2/16/00	4/18/01	4/1/01	$1,293††
Unsub	3/7/00	4/18/01	4/1/01	$1,293††
Sub	3/7/00	4/18/01	4/1/01	$848†
Sub		11/16/01	1/1/00	($1,696)†
Unsub		11/16/01	1/1/00	($2,586)††

* Adjusting Entry as a result of Pell reconciliation

** Refund paid to ED

† Reversing Entry (Sub)

†† Reversing Entry (Unsub)

The combined transactions at the Riverdale and Atlanta campuses resulted in the student receiving the following Title IV funds amounts:

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Program	Amount
SEOG FCC	$ 60
Pell	$3,125
Subsidized Stafford	$2,545
Unsubsidized Stafford	$1,737

The student began classroom attendance November 1, 1999 at the Riverdale campus and attended that campus through March 10, 2000. The student attended the Atlanta campus March 13, 2000 through his graduation date of July 25, 2000. The student did not interrupt his attendance at either campus. The "Drop" designation at the Riverdale campus reflected the student's transfer to the Atlanta campus.

The SEOG ($60), Pell ($3,125), and Subsidized Stafford ($2,545) were credited to the student's account promptly and before the student's last date of attendance. ACT requests that these amounts be deleted from the Final Audit Report.

The student was also eligible for the $1,737 in Unsubsidized Stafford funds when they were drawn down in February and March 2000, which was well before the student's graduation date and last date of attendance.

8.

ACT believes the Draft Audit Report did not take into consideration an Unsubsidized Direct Stafford Loan reconciliation adjustment in the amount of $1,294 indicated by a transaction date of 1/1/00 entered 11/13/01. This transaction is the first entry on the student's ledger card, and is a reversal of the 1/18/01 (transaction date) entry identified as "Direct Unsub 1999-00" in the amount of $1,294. The student's account indicates total Unsubsidized Stafford Loan credits, net of the reconciliation adjustment, of $2,588. This amount corresponds to the $2,666 (gross) unsubsidized loan amount indicated on the NSLDS Loan Summary. See Exhibit 3-A for a copy of the ledger card and NSLDS Loan Summary for this student.

In summary, as noted above, ACT believes that some of the questioned funds for these eight students were timely and properly disbursed, and should be deleted from the Final Audit Report. ACT has also demonstrated that the cited students were enrolled and eligible for most of the remaining funds at the time the funds were drawn down from ED, and the only problem was the institution's tardiness in actually crediting the funds to the students' accounts. The institution suggests that, in these circumstances, it not be penalized in both Finding No. 2 and again in Finding No. 3 for the same issue, and requests that these liability amounts be deleted from Finding No. 3 in the Final Audit Report.

B. Disbursements After Student's Last Date of Attendance

The Draft Audit Report cites ACT for making second Direct Loan disbursements to two students after their last date of attendance even though the students withdrew before the end of the payment period for which the loan disbursement was applicable. Following is an explanation of the circumstances for each of these students.

1.

This student was awarded a Subsidized Direct Stafford Loan for her seven-month program of study. The first disbursement of $1,274 is not in question. The student completed one half of her program February 22, 2001. The student withdrew from the institution with a drop determination date of August 22, 2001 and a last date of attendance of June 1, 2001.

ACT records indicate that $1,273 for a Subsidized Direct Stafford Loan was drawn down June 1, 2001 and intended for payment of the second disbursement on the student's loan. The funds in question were credited to the student's account July 2, 2001 (post date) and a transaction date of June 1, 2001. The student was eligible for the second disbursement when it was drawn down on June 1, 2001, but had withdrawn by the date the disbursement was credited to her account.

The student eventually returned to school and graduated March 13, 2003. Thus, she was ultimately entitled to the amount of the second disbursement, and ACT requests that the OIG not include this as a recommended liability amount.

2. –

The student was awarded a Subsidized Direct Stafford loan and an Unsubsidized Direct Stafford Loan for her seven-month program of study. The first disbursements of each loan are not in question. The student completed one half of her program December 3, 1999. The student withdrew from the institution with a drop determination date of January 10, 2000 and an LDA of December 20, 1999.

ACT records indicate $849 for a Subsidized Direct Stafford and $1,293 for an Unsubsidized Direct Stafford were drawn down December 20, 1999 and were intended for the second disbursements on the student's loans.

The funds in question were credited to the student's account on January 11, 2000 (post date) and a transaction date of December 20, 1999. The student was eligible for the second disbursement on each loan when they were drawn down on December 20, 1999, but had withdrawn by the date the loan amounts were credited to her account. As with the students in the preceding group, ACT requests that the recommended liability amount for this student be deleted in the Final Audit Report.

C. Missing File

The Draft Audit Report recommends a liability for all of the Title IV funds received on behalf of one student whose file ACT was unable to locate during the site visit. ACT has subsequently located the student's file, and a copy of it is attached as Exhibit 3-B. ACT requests that this student and the associated liability amount be removed from the Final Audit Report.

D. Students Who Did Not Pass the Ability-to-Benefit Test

The Draft Audit Report recommends a liability for Title IV funds received on behalf of five students for whom ACT could not provide documentation that the student had passed the Wonderlic ability-to-benefit test.

ACT has reviewed the files of each of these students. One of the students received a G.E.D. diploma, a copy of which is attached as Exhibit 3-C. For that reason, there should be no liability for this student.

For the remaining four students, ACT has been unable to document that the student passed the ATB test. However, three of these students completed their program of study and graduated from ACT. Attached as Exhibit 3-D are copies of the academic transcripts for these three students, indicating their completion of program and graduation. ED has a longstanding practice of not assessing liability against an institution for a student who was improperly admitted under the ability-to-benefit option if the student ultimately completed his or her educational program and graduated from the institution. It is ACT's understanding that the reasoning behind this approach is that if a student completes the educational program, then by definition he or she had the ability to benefit from the program. This practice has been used many times by ED. Therefore, ACT requests that the OIG not recommend any repayment liability in the Final Audit Report for these remaining four students.

With respect to the OIG's two recommendations concerning Finding No. 3 of the Draft Audit Report, ACT has addressed above each of the specific recommended liability amounts (Recommendation 3.1). Recommendation 3.2 states that ACT should address confusion among the school's financial aid personnel regarding their responsibilities to ensure that ineligible students do not receive Title IV disbursements. As stated elsewhere in this response, ACT has implemented various new procedures and has provided additional training to its staff, to ensure that Title IV funds are not disbursed to ineligible students.

In addition, ACT would like to call the attention of the OIG to the fact that the institution's annual compliance audit for the fiscal year ending December 31, 2002, which was recently completed, did not identify any instances of non-compliance during 2002 for any of the issues for which students were cited in Finding No. 3 of the Draft Audit Report.

Finally, ACT wishes to advise the OIG that ACT is discontinuing use of ability-to-benefit testing for admitting new students. Effective June 1, 2003, new applicants to ACT will only be admitted if they have a high school diploma or G.E.D. certificate.

Finding No. 4: ACT Did Not Reconcile Direct Loan Funds

The Draft Audit Report states that ACT did not reconcile its 1998-99 and 1999-2000 Direct Loan awards on a monthly basis.

ACT agrees that during that period of time, it was not reconciling its Direct Loan accounts on a monthly basis. However, subsequent to that time -- and before the OIG began its audit -- ACT initiated a reconciliation of its Direct Loan funds. As a result of that reconciliation, ACT returned excess cash funds to ED, as acknowledged in the Draft Audit Report.

The enclosed documents received from ED on June 2, 2003 (see Exhibit 4-A) confirm an ending cash balance for the 1998-99 year of $0.50, a final figure ACT is very pleased with.

The enclosed ED Direct School Loan Account Statement dated April 10, 2002 (see Exhibit 4-B) confirms an ending cash balance for the 1999-2000 year of negative $3.00, meaning ACT had undrawn Direct Loan cash needs of $3.00.

In April 2000, ACT engaged Global Financial Aid Services to perform a variety of Title IV cash management functions for the school. One of the services Global performs on behalf of ACT is the reconciliation of Direct Loan transactions. Global began conducting complete monthly reconciliations of Direct Loan funds at the beginning of the 2000-01 school year, and continues to do so to this date. Global performs the reconciliation, reports to ACT management, and works directly with ED on any questions. The Draft Audit Report confirms that Global has policies and procedures in place for reconciling ACT's Direct Loan funds on a monthly basis, and that Global was following its procedures and conducting the reconciliations as required.

ACT is happy to emphasize that the failure to reconcile Direct Loan funds on a monthly basis is a problem of the past that has been rectified.

The first recommendation in the Draft Audit Report concerning Finding No. 4 is for ACT to train personnel in the reconciliation requirements of the Direct Loan program. ACT personnel are now fully aware of the monthly reconciliation requirements, and the staff performing the reconciliation (i.e., Global) are fully trained, very experienced and very capable to perform those duties. The second recommendation for Finding No. 4 is that ACT should monitor its third-party servicer's performance to ensure continued compliance with program requirements. ACT works closely with Global on a daily basis. While ACT does not itself audit Global's Direct Loan reconciliations, it does monitor Global's performance of the reconciliations, which continue to show that the accounts are being properly reconciled.

Finding No. 5: ACT Failed to Properly Calculate or Make Refunds For Students Who Withdrew

The Draft Audit Report states that ACT failed to make refunds for 11 students, and incorrectly calculated refunds for two other students, who withdrew during academic years 1999-2000 and 2000-01, and that ACT owes ED $10,112 in refunds for these students.

ACT has carefully reviewed the files of the 13 students identified by the OIG. For each of the students, ACT has performed a new Return to Title IV (R2T4) calculation.

1.

The recalculated R2T4 indicates a return of funds in the amount of $988.75. ACT records indicate a R2T4 was calculated 11/30/01 in the amount of $988.75 to be returned to the Pell Grant Program. For unknown reasons, the funds were not returned at the time of the calculation. Subsequently, the funds were returned on 6/17/03. The relevant documentation for this student is included in Exhibit 5-A.

2.

The recalculated R2T4 calculation (Exhibit 5-B) indicates the student attended 65% of the payment period and therefore earned 100% of the funds received.

3.

The recalculated R2T4 includes Title IV aid that "could have been disbursed" in the amounts of $1,940 and $1,274 in Stafford loans, which were electronically originated 12/20/00, prior to the student's withdrawal date. Thus, this student earned 100% of the funds disbursed. The documents for this student are included in Exhibit 5-C.

4.

ACT records indicate a R2T4 was calculated 12/12/01 in the amount of $1,267.30. For unknown reasons, the funds were not returned at the time of calculation. The funds were returned 6/16/03 (Exhibit 5-D).

5.

The recalculated R2T4 includes Title IV aid that "could have been disbursed" in the amounts of $1,940 and $1,274 in Stafford loans, which were electronically originated 2/20/01, prior to the student's last date of attendance. Thus, this student earned 100% of the funds disbursed. The documents for this student are included in Exhibit 5-E.

6.

The recalculated R2T4 includes Title IV aid that "could have been disbursed" in the amounts of $1,940 and $1,274 in Stafford loans, which were electronically originated 10/18/00, prior to the student's LDA. The "could have been disbursed" amount also includes $60 in SEOG. The calculation indicates the student earned 100% of funds disbursed. The documents for this student are included in Exhibit 5-F.

7.

The recalculated R2T4 includes Title IV aid that "could have been disbursed" in the amounts of $1,940 and $1,274 in Stafford loans, which were electronically originated 2/8/01, prior to the student's LDA. Thus, this student earned 100% of the funds disbursed. The documents for this student are included in Exhibit 5-G.

8.

The school's records indicate that its third-party servicer (Global) performed a R2T4 calculation on 3/12/01, which indicated no return of funds. This calculation included Title IV aid that "could have been disbursed" in the amounts of $1,274 in Subsidized Stafford and $2,925 in PLUS, which were electronically originated 2/15/01 and 2/19/01, respectively.

Current information indicates the PLUS was denied, presumably after the Global calculation. The recalculated R2T4 thus excludes PLUS as a "could have been disbursed" amount, which results in $842.80 to be returned to the Pell Grant program. The funds were returned 6/18/03. The documents for this student are included in Exhibit 5-H.

9.

ACT's records indicate that its third-party servicer (Global) performed an R2T4 calculation (Exhibit 5-I) on 2/5/01 which required a Return to Title IV of $2,304. For unknown reasons, the funds were not returned at that time. The student re-enrolled on 8/20/01, and therefore regained eligibility for the funds that should have been returned, and graduated on 10/19/01.

10.

ACT's records indicate that a Stafford loan in the amount of $1,274 was electronically originated 2/8/01 and a PLUS loan in the amount of $2,924 was electronically originated 2/12/01. In addition, a Pell Grant for $1,650 and a SEOG for $100 were disbursed prior to the student's last date of attendance (3/23/01). A R2T4 calculation utilizing the above activity would have indicated the student had earned 100% of the funds disbursed.

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Current information indicates the PLUS loan was ultimately denied. The recalculated R2T4 excludes the PLUS from the Title IV aid that "could have been disbursed" but includes the Stafford as aid that "could have been disbursed" and results in a R2T4 of $156.35 to the Pell Grant program. The funds were returned 6/18/03. The documents for this student are included in Exhibit 5-J.

11.

ACT records indicate the student withdrew from school on two previous occasions (LDA 11/30/00 and LDA 1/25/01). A R2T4 calculation for each of the two prior withdrawals indicated the student earned 100% of the funds disbursed.

The student last withdrew from school with an LDA of 6/15/01. A R2T4 calculation was performed 7/19/01 and indicated the student had earned 100% of the funds disbursed for the payment period. The recalculated R2T4 confirmed the student earned 100% of the funds disbursed for the payment period. The documents for this student are included in Exhibit 5-K.

12.

ACT's records indicate a R2T4 calculation was done 6/28/01, which indicated a R2T4 of $2,131.50 was required. This amount was returned to the Stafford Loan program. In addition to the required R2T4, the institution returned an additional $150 in SEOG FCC.

The recalculated R2T4 confirmed the accuracy of the original calculation which required $2,131.50 be returned. The documents for this student are included in Exhibit 5-L.

13.

ACT's records indicate a R2T4 calculation was performed 7/3/01, which indicated a R2T4 of $1,529.86 was required. This amount was returned to the Stafford Loan program.

The recalculated R2T4 confirmed the accuracy of the original calculation. The documents for this student are included in Exhibit 5-M.

As a result of the R2T4 recalculations for the above 13 students, ACT has now paid the additional $3,255.20 for the four students which ACT determined was still due.

The Draft Audit Report notes that ACT has had late and unmade refunds in the past, a fact that ACT readily admits. ACT has performed extensive file reviews over a period of several years, under the direction of ED's Atlanta Case Management Team, to identify additional refunds that were not paid correctly and timely. ACT has paid all additional refund amounts identified by those file reviews, and the Case Management Team has closed the compliance audits for those years.

ACT is very pleased to report to the OIG that its independent auditor's Title IV compliance attestation report for ACT's fiscal year 2002 identified only one late refund and no unmade refunds in its audit sample. Therefore, ACT believes, as with certain other issues identified in the Draft Audit Report, that ACT's refund problem is a problem of the past that has been cured.

As an additional matter, ACT would like to inform the OIG that it has already been assessed an administrative fine by ED's Administrative Actions and Appeals Division for the school's failure to pay refunds in a timely manner for the school's fiscal years ending October 31, 1999, October 31, 2000, and October 31, 2001, and the stub fiscal year period ending December 31, 2001. ACT has paid the fine amount as agreed to with ED, and that matter is now closed. A copy of the Settlement Agreement reflecting closure of that proceeding and payment of the fine are attached as Exhibit 5-N.

There are three recommendations in the Draft Audit Report for Finding No. 5. Recommendation 5.1 is that ACT refund to ED $10,112 for the refunds not made or made in the incorrect amount. As indicated above and as supported by the attached documentation, ACT believes that the correct amount of additional refunds due is a total of $3,255.20 for four students, which ACT has fully paid, prior to submitting this response.

Recommendation 5.2 is that ACT implement policies, procedures and management controls to ensure the accurate calculation of refunds and the timely return of such funds to ED. ACT has developed and now has in place detailed policies and procedures for ensuring refunds are correctly and timely made. Attached as Exhibit 5-O is the Refunds section of ACT's Policies and Procedures Manual, which sets forth in detail the school's processes in this regard. As noted above, due to the implementation of these procedures, ACT was cited for only one late refund in its 2002 annual compliance audit.

Recommendation 5.3 is that ED should either fine ACT or limit, suspend or terminate ACT's participation in the Title IV programs due to its failure to make refunds. For all of the reasons set forth above, including most importantly that ACT has eliminated its refund problem and has already paid a substantial fine to ED for the same years covered by the Draft Audit Report, ACT believes that no additional adverse action against it is warranted. ACT respectfully requests that Recommendation 5.3 be removed from the Final Audit Report.

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Finding No. 6: ACT Did Not Demonstrate Administrative Capability

In Finding No. 6, the Draft Audit Report states that, on the basis of the issues identified in Finding Nos. 1-5, as well as a high turnover in financial aid staff, ACT did not meet ED's required standards of administrative capability. Finding No. 6 does not include any additional items that are not included within the other previous findings.

ACT has addressed each of the other findings above. While ACT acknowledges that it had certain administrative and cash management problems in the past, ACT has also tried to demonstrate that it has devoted extensive attention and resources to correcting these problems. The problems identified in the Draft Audit Report have been addressed and have been either completely or largely corrected.

ACT has addressed its past high turnover rate for financial aid staff in two primary ways. First, ACT brought in Global Financial Aid Services to perform many of the financial aid functions for the school. Global is a very stable company with very experienced staff and an extremely low rate of error. Second, ACT has increased its training of its own financial aid employees, to help ensure that any mistakes by them are minimized. This training has been provided by senior management at the school, by personnel from ACT's parent company, and by Global, and has covered the issues identified in the Draft Audit Report and many other areas. ACT believes that this increased training has provided much improved results.

ACT also believes that the results of its annual compliance audits are relevant to this issue. Those audits show a distinct improvement in the magnitude and type of finding identified by the auditors. While not perfect (as virtually no school is), ACT's most recent audits do show very marked improvement and a very greatly reduced error rate, further attesting to its current administrative capability.

Based on the corrective actions that it has taken to address the issues identified in the findings of the Draft Audit Report, and its current capabilities and processes, ACT does not believe that it should be limited, suspended or terminated from future participation in the Title IV programs. ACT requests that Finding No. 6 be eliminated when the OIG issues its Final Audit Report.